DUBLIN AIRPORT

Response to Issues Paper CP7/2018

13 July 2018

Contents

1. Introduction

1.1 We welcome the opportunity to respond to the Commission for Aviation Regulation's ('the Commission') 2018 Issues Paper. The Issues Paper, published 30 April 2018 and titled *2019 Determination Maximum Levels of Airport Charges at Dublin Airport CP7/2018* represents the beginning of the Commission's process of engaging with stakeholders in preparation for the 2019 Determination.

1.2 We acknowledge that the Commission initially provided stakeholders with almost nine weeks to respond to this consultation on 29 June but subsequently extended this period on 19 June by two weeks to 13 July 2018. It is not clear why this two-week extension was provided to stakeholders but we have availed of this extension nonetheless.

1.3 The Commission's Issues Paper covers many key topics that are worthy of consideration in advance of the 2019 Determination. The timing surrounding the consultation on the Issues Paper is somewhat concerning however. We are concerned that the Commission will consult on key issues in April 2018 and that stakeholders will not hear from the Commission on these matters until a year after this date i.e. April 2019.

1.4 By the time the Commission publishes its Draft Decision (expected April 2019), this will essentially represent yet another consultation on key issues. It is unusual and unhelpful for a consultation process to span such a long timeframe and without the provision of certainty or guidance from the Commission on the relevant parameters in the meantime.

1.5 During this time between the Commission's April 2018 and April 2019 consultations, Dublin Airport will have carried out its own consultations with airport users on key issues such as passenger forecasting methodology, service quality metrics and the Capital Investment Programme ('CIP') before submitting an all encapsulating regulatory proposition to the Commission at the end of 2018.

1.6 It is especially concerning that there are so many regulatory hurdles in advance of the 2019 Determination in which a significant burden of proof is placed upon Dublin Airport.

1.7 Furthermore, the Commission does not appear to consider the cost of effectively engaging in its regulatory process nor has the Commission considered the scope that exists for genuine oversight from Dublin Airport due to, for example, tight timelines

for tweaking our regulatory proposition having considered the views of airport users in the responses to our consultation. The Commission will recall that upon receipt of responses to the Programme of Airport Campus Enhancement ('PACE') consultation in November 2017, Dublin Airport increased the suite of projects by 7 from 16 to 23 for inclusion in our December 2017 submission to the Commission. Similar timelines will apply later in 2018 with respect to the CIP, which is expected to be substantially more detailed than PACE. However, any changes following consultation may have important implications for other building blocks such as the commercial revenue target or the operating expenditure target. A period of four to six weeks (i.e. in between the conclusion of our CIP consultation and the submission of our Regulatory Proposition) may be insufficient to comprehensively finalise our Regulatory Proposition.

1.8 The process surrounding the build up to the 2019 Determination and general timelines are very similar to the 2014 Determination but the Commission will be aware that the scale of the 2019 Determination – both from the level of investment required and volume of passengers – is far greater than previous years. Consequently, there is an increased risk that either Dublin Airport or the Commission will not capture relevant information in the 2019 Determination, which could prove very costly to Dublin Airport over the period 2020-2024 (assuming the duration of the 2019 Determination does not change).

1.9 While previous Determinations from the Commission represent important milestones in time and particularly the most recent 2014 Determination, Dublin Airport strongly believes that aspects of this Decision including certain benchmarks were inappropriate and are even more inappropriate in preparing the review period 2020-2024. In the 2014 Determination the Commission considered, for example, our operating expenditure per passenger with the equivalent metric in Ryanair served European airports. We are not comparable with this overall profile of airports and this blended suite of airports operating expenditure should therefore not influence the prospective target for operating expenditure at Dublin Airport.

1.10 It is against this backdrop that we would not agree with the Commission's view in paragraph 1.6 that "*…incentive based regulation [is] working as intended*". We do not agree that the considerable deficit in our operating expenditure allowance compared to actual incurred operating expenditure represents effective incentive based regulation as we believe this target set in 2014 was too onerous and should have been considered objectively and in isolation from the potential (and incentives) to outperform on other building blocks. In this regard, we welcome the assertion from the Commission that "*an assessment of what worked well and what did not*" is required. As previously noted, there are two necessary conditions in order for an incentive to be real and positive: (i) we must have some meaningful control over the

variable in question and (ii) there has to be a realistic possibility of achieving upside relative to the Determination forecast.

1.11 In addition, we do not consider incentive based regulation to be effectively in place when we are incurring costs (e.g. Hold Baggage Screening 'HBS' operating expenditure) without any allowance. Had Dublin Airport sought an interim review in this regard, we understand it may have led to unintended consequences but it is not clear why our ability to outperform on unrelated building blocks, as we have been incentivised to do, should be affected by mandated costs (mid-Determination) that we have no control over. Again, for reasons such as this, we welcome the assertion from the Commission that "*an assessment of what worked well and what did not*" is required.

1.12 We note that a key theme of the Commission's 2019 Determination will involve "*balancing the competing needs of a flexible regulatory model with one which has strong efficiency incentives*". It is difficult to know what this means in practice and what bearing (if any) this will have on the approach to the next Determination compared to the existing Determination. We wish to note that the regulatory model in its current form is quite rigid and that our existing allowance for operating costs is more closely aligned to a hypothetical efficient new entrant rather the reality of what needs to be incurred by Dublin Airport.

1.13 In setting out our views on key issues at this point in time, we have endeavoured to follow the sequencing of the Commission's Issue Paper. Confidential information will be redacted in a non-confidential version and marked with ✂ [redacted].

2. Policy Developments since the 2014 Determination

2.1 The Commission notes that some of its key strategic questions will be informed by Government policy and further notes that the National Policy Statement on Airport Charges Regulation has reaffirmed the need for price cap regulation at Dublin Airport. Planned changes to the regulatory framework are also outlined.

2.2 The proposals contained within the 2017 National Policy Statement on Airport Charges Regulation are fuelling considerable uncertainty as it is not known if the recommendations will be enacted before the 2019 Determination and if so, how it will affect the Determination (if at all). We request that the Commission provides stakeholders with updates on any developments in this regard during the remainder of 2018 and in 2019.

2.3 There are many aspects of the National Policy Statement that we require clarity on in the context of the 2019 Determination and in advance of our own consultations. For example, the question of whether the Commission will have regard to the chapter on sustainability and responding to climate change is significant from the perspective of certain plans that we have in this regard.

2.4 Dublin Airport does not agree with a conclusion "*that regulation of Dublin Airport will continue, in recognition of its significant market power*". We do not agree that this conclusion would follow in the absence of a robust market analysis that has been the subject of extensive consultation. Such a market analysis would have first defined the relevant market being considered and it is not a foregone conclusion that the island of Ireland is the relevant market given the extensive competition that we face beyond the geographic boundary (e.g. Keflavík, Heathrow and Schiphol as detailed below). A subsequent market analysis of the relevant market(s) should subsequently have considered the ability of airlines to switch airports, countervailing buyer power, the availability of substitutes and the intensifying competition with major international hubs for transfer passengers.

2.5 We are of the view that the Commission should have considered the recent work by the European Commission and its consultants SDG with regard to the Airport Charges Directive ('ACD') and the associated shortcomings that are ultimately driving a review of the Directive. The timelines and implications of this review are relevant in the context of the next Determination as it is likely that a review would take place mid-Determination.

2.6 In December 2017, daa responded to a EC consultation regarding the ACD by noting that we are opposed to any measures that:

- hinder the development of competition and scope for commercial agreements with customer airlines;
- assume Significant Market Power ('SMP'), without a robust and comprehensive assessment;
- consider continued reduction in airport charges to be the sole remedy at the disposal of regulators;
- ignore proven alternative remedies such as transparency, ex-post monitoring, bi-lateral agreements and other tailored solutions.

2.7 We also noted that we face increasing competition for transfer services from European airports such as Reykjavik's Keflavík International Airport, London's Heathrow Airport and Amsterdam's Schiphol Airport. For example, Keflavík has experienced growth of 281% between 2010 and 2016 and has strong transatlantic connectivity, served by airlines such as Icelandair and WOW. Transatlantic flights represent 32% of the overall market of Keflavík (compared to 11% of the overall market of Dublin) which, along with its geographical position, makes Reykjavik a strong competitor for transfer business. It is our view that airport competition will further increase in the future, as Low-Cost Carriers ('LCC') move into long-haul operations and Full-Service Carriers respond by becoming more flexible & embracing LCC models.

2.8 Oxera has recently assessed competition between airports in Europe and found that there is significant and growing competition, which may indicate that less, and/or less intrusive regulation, would be appropriate.[1] Furthermore, there are now many more airports facing competitive constraints that are subject to this European-wide scheme of regulation compared to when the ACD was implemented and often in addition to economic oversight applied at the national level.

2.9 Oxera's report[2] on 'Market power assessments in the European airports sector' sets out how to determine whether an airport has SMP. It establishes a three-stage process, which includes a two-stage SMP test and a third stage on the design of regulation according to the degree of market power of the firm. Furthermore, an

[1] Oxera (2017), 'The continuing development of airport competition in Europe', prepared for ACI EUROPE, 26 September.

[2] Oxera (2017), 'Market power assessments in the European airports sector', Prepared for ACI Europe, 13 October.

Oxera note dated 15 May 2018 and titled "*Best practice in developing economic oversight for airports*" detailed the following three steps:

Step 1

This involves an assessment of whether the firm has significant market power, and if so, the degree of market power. This step also requires a consideration of the risk of the abuse of that market power and whether any potential abuse could be dealt with effectively through competition law.

It follows that if competition law is determined not to be sufficient, an assessment of the costs and benefits of regulation would be required as regulation should only be introduced if there is a net benefit from doing so[3].

Step 2

The second step is to determine how to regulate and the appropriate form of intervention in the market could take many forms—such as an Authority intervening to promote competition, or more formal monitoring of the behaviour of a firm. As in determining whether to regulate, in this step it is important to consider the risk of abuse of SMP, assess whether competition law is sufficient, and compare the costs and benefits of different forms of regulation in deciding on the appropriate remedy.

Step 3

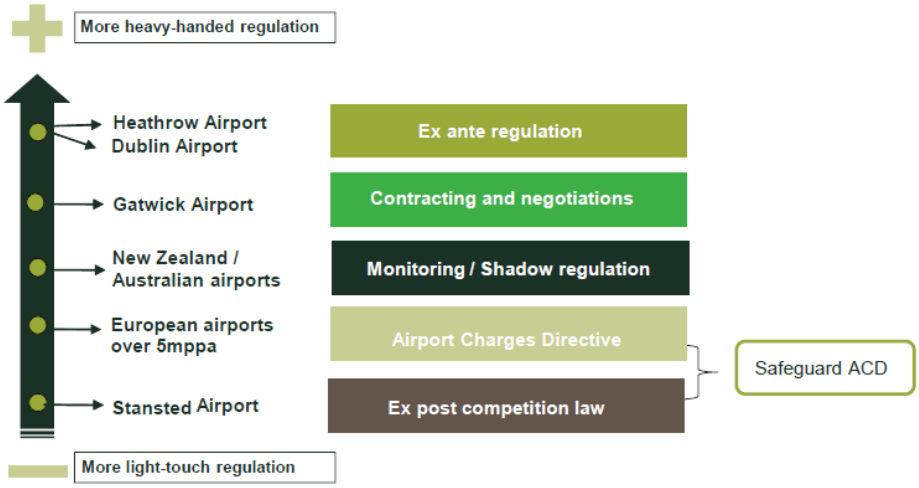
The regulatory framework and associated remedies should be tailored to reflect the nature and level of market power (if any) possessed by Dublin Airport. Many options exist in this regard and one option would be to safeguard the ACD, where there is limited dominance or SMP. It would involve keeping the principles of transparency, non-discrimination and consultation and would ensure that there are some 'rules of the game' set out for interactions between airlines and airports. Ultimately it would facilitate a setting that builds confidence between parties as the competitive market continues to develop.

2.10 Another lighter touch option would be monitoring or shadow regulation which represents a lighter touch regulatory regime whereby the regulator would delegate

[3] It is worth noting that the National Policy Statement on Airport Charges or the Commission's Issues Paper have not considered any such costs of regulation such as (i) crowding out of a commercial approach, (ii) management distraction, (iii) the impact on developing competition, (iv) the rigidity of the regulatory system and the potential for suboptimal calibration of incentives.

responsibility for pricing arrangements to the company. Under such a framework, the regulator would regularly monitor price and service quality outcomes to ensure that there is some ex ante action taken by the regulator in 'setting the rules of the game' with respect to information and pricing principles.

Table 1: Range of remedies to be considered for Dublin Airport



Source: Oxera

2.11 There are two key factors to consider in determining whether competition law would provide sufficient protection against an abuse of market power: assessing whether there are any constraints on the abuse of market power, and the economic consequences of abusing that market power. In the UK Civil Aviation Authority's three-part test framework, even if an airport has SMP then if competition law provides sufficient protection against the risk of abuse of SMP (Test B) regulation would not be introduced. Similarly, the European Commission applies three cumulative criteria for determining whether an electronics communications market 'is susceptible to ex ante regulation'. One of these conditions is whether competition law is sufficient to address market failures.

2.12 We are of the view that the Commission should have due regard for a recent statement by Alexandre de Juniac, the Director General of IATA, which suggests that *"Regulators must recognise the power of competition" and "Governments should not distort market effectiveness with regulations that second guess what consumers want".*

2.13 Other policy developments from the EU and Brexit are addressed in Sections 4.5 and 6.5.

3. The Commission's approach to regulation at Dublin Airport

3.1 Strategic considerations regarding capacity

3.1 We agree that capacity is now scarce at Dublin Airport and passenger welfare is not well served by a capacity constrained airport. Does this imply that the Commission is prepared to support a proposal that provides for sufficient headroom and the benefits this can lead to? It is not clear to Dublin Airport at this point in time what the view of the Commission is in this regard as the Commission also notes that "*if you over provide infrastructure the risk of being constrained is lower, but users may be paying for infrastructure they do not need at a particular point in time*".

3.2 In paragraph 4.11 the Commission has requested that long term strategic questions should be considered in a deliberative process that engages all stakeholders. There is no doubt that the Commission is implicitly referring to the Masterplan process at Dublin Airport. However, while the Commission is aware of ongoing developments surrounding the Masterplan and the exertion of countervailing buyer power in this regard, it will also be aware of the time constraints underpinning the regulatory process and the urgent need to deliver capacity post 2020.

3.3 Consequently, there has been much focus on the more medium to long term requirements (out to 40 million passengers per annum) that are compatible with a longer-term strategy (out to 55 million passengers per annum and beyond). However, the Commission will be acutely aware that it is not practical or feasible for Dublin Airport to consult on a wider Masterplan in conjunction with the many other consultations required in advance of our regulatory submission to the Commission later this year.

3.4 A crucial issue that the Commission has not considered is that for Dublin Airport to undertake a meaningful consultation on its Capital Investment Programme, it must be willing to take on board views of airport users and tailor this programme accordingly – in the presence of significant countervailing power from key customers, this could potentially lead to a suboptimal outcome and we would welcome the views of the Commission in this regard.

3.5 Addressing the issue of capacity constraints at the Airport requires a more strategic long-term view to airport planning which has been at odds in the past with the more short-term focus of airport users in the past and the medium-term priorities of the regulatory framework. What this means in practice from the Commission's

perspective and in the context of the 2019 Determination is not quite clear as we prepare for key consultations with airport users in Q3 2018.

3.6 We address our concerns in this regard in the section on capital expenditure (see Section 7).

3.2 The relationship between service quality and cost

3.7 The Commission notes in paragraph 4.6 that there is a trade-off between quality and cost. It further notes that the relationship between quality and price is less obvious, as lower quality services may lead to reduced volume, and given the high level of fixed costs at an airport could lead to an increased price cap. The Commission concludes that the desired quality level is a choice but one which has consequences for the regulatory building blocks.

3.8 We would question how the Commission will address the trade-off between service quality and cost in the forthcoming Determination, or what its preliminary views are in this regard. We consider it to be one of the most important questions for the 2019 Determination and we are of the view that this single paragraph 4.6 of the Issues Paper specific to service quality and the Commission's approach to regulation is so speculative and vague that it provides no certainty or guidance whatsoever.

3.9 Throughout 2017 and earlier this year we have engaged with the Commission on a number of its consultations relating to passenger representation and service quality and we have repeatedly sought further clarity from the Commission.

3.10 We request that the Commission does its utmost to communicate its preliminary views as comprehensively as possible and in a timely manner in advance of the next Determination, given the significant time constraints that we are faced with.

3.11 We address the important relationship between service quality and cost in Section 5 on operating expenditure and further discuss the relevance of service quality in Section 10.

3.3 Differentiated Services

3.12 There has been a range of different business models in place at Dublin Airport for quite some time but the Commission is right to point out that the variance is increasing, particularly with the arrival of two Asian carriers this year and a more diverse passenger profile arising from this, in addition to our transfer business.

3.13 Regarding the Commission's follow on question as to whether Dublin Airport should have differentiated passenger service charges depending on whether the passenger is using Terminal 1 or Terminal 2, we wish to note that our airport charges are subject to

consultation each year with airport users and with oversight by the Commission. We can only infer whether the Commission is suggesting that the use of Terminal 1 would result in a lower passenger charge compared to Terminal 2 due in part to the age, for example – we would welcome a more comprehensive preliminary view from the Commission in this respect and its preferred approach in making such an assessment.

3.14 We would also welcome a more comprehensive discussion on what represents differentiation. For example, is the Commission of the view that in a single till regulatory environment, the varying commercial value of passengers and associated operating costs would need to be evaluated also? In addition, if we have no discernible difference in quality of service between terminals, how would the Commission set about demonstrating that there is a different offering.

3.15 An issue the Commission would have to consider is the charge for those transfer passengers who avail of both terminal buildings. In consulting on our airport charges in 2017 we did not receive any specific objection to setting a passenger charge that does not reflect terminal differentiation.

3.4 Form and duration of the price cap

3.16 The Commission has noted that it has discretion on the form and operation of the price cap and accordingly has been setting a maximum average charge per passenger to date. We would ask that the Commission considers alternative, more lighter touch, options that are compatible with its statutory remit. Such options would not simply be limited to facilitating bilateral contracts. Thought should be given to lighter touch options in the event that bilateral contracts do not materialise.

3.17 We note that the 2019 Determination must last for a minimum of four years but we have nonetheless commenced preparations on the basis that it will cover the period 2020-2024 at a minimum. We would welcome clarity on this from the Commission in advance of our Capital Investment Programme consultation this September.

3.5 Risk Allocation

3.18 We welcome acknowledgement from the Commission in relation to the significant risks facing Dublin Airport in the 2019 Determination.

3.19 We agree with the Commission that there are two key mechanisms which allocate risk to the airport, including volume risk and the absence of ex post adjustments to Opex, commercial revenue and cost of capital. While these risks will be similar in principle compared to previous Determinations, the scale of our operation and required investment means that we are facing disproportionately higher risks in the 2019

Determination and are consequently more financially exposed than previous years – that is, unless the Commission can set reasonable targets and ensure that we are sufficiently remunerated for efficient operating expenditure incurred (e.g. mandated security costs), which may take the form of an ex ante allowance (based on extrapolating similar costs from previous years) or an ex post adjustment.

3.20 However, we wish to emphasise that there is a third key mechanism specific to the allocation of risk in the form of ex ante capital investment allowances. There are a number of different types of risk associated with these prospective allowances and given the projected scale of our capital allowance in September 2019 (which will be based on December 2017 estimations), it is possible that the projected capital costs will fall short of what is actually required and supported by airport users.

3.21 The nature of the risk attached to the capital allowances if addressed in Section 7 overleaf and covers issues relating to construction inflation, contingency/escalation allowances being absorbed by efficient cost-overruns, and the possibility that the level of design will be insufficient to reliably inform cost estimates for any projects that are late additions to our Regulatory Proposition following airline support.

3.22 A good example that demonstrates the magnitude of risk associated with capital allowances is the north runway which received an allowance from the Commission of €247 million in 2014 but is likely to exceed this original estimate by more than €70 million when competitive dialogue is completed later this summer. While the Commission provided the Airport with an opportunity to re-consult on these costs in 2017, we were of the view that even three years following receipt of the allowance, it was too soon to have a meaningful consultation on the appropriate level of costs as the competitive dialogue procurement process had only commenced that year and was not scheduled to complete until mid-2018.

3.6 The Commission's High-Level Methodology (i.e. building blocks approach)

3.23 We are preparing for the 2019 Determination on the basis that there will not be any significant deviations in the Commission's building blocks approach to RAB based regulation when setting the price cap. We are preparing accordingly because we have not received any signal to suggest the Commission is prepared to improve this high-level methodology. Despite the question on this in the Issues Paper, we are not convinced that scope exists for any change.

3.24 Firstly, we would have appreciated some insight from the Commission on whether it is minded to improve this methodology rather than simply have included an open ended question. Secondly, alternative options presented by the Commission would create a

more meaningful process. Finally, it is disconcerting that the Commission has noted any move away from this high-level approach would require careful consideration and deliberation with all interested parties – this question is already contained within a lengthy consultation that feeds into at least one further consultation next year and the prospects of having a further consultation on this issue is unsettling, given the time constraints and limited information provided at this point in time.

3.25 We address the importance of setting reasonable targets across the various building blocks in the relevant sections overleaf.

4. Passenger Targets set by the Commission

4.1 High level consultation questions on setting passenger targets

4.1 In section 5 of the Issues Paper consultation, the Commission asks stakeholders about the most appropriate methodology and data sources for projecting passenger numbers at Dublin Airport, in addition to whether the forecast should be aggregate or disaggregated. These questions will be the subject of a Dublin Airport led consultation with airport users and the Commission in a matter of weeks and the outcome of this consultation will be included in our Regulatory Proposition submitted to the Commission later this year.

4.2 Capacity and planning constraints

4.2 Notwithstanding our impending consultation on passenger forecasting it is imperative that the Commission gives due consideration to the capacity constraints at the Airport, which are unlikely to be fully alleviated until the suite of PACE projects and the next capital investment plan are rolled out.

4.3 The Commission also needs to have regard for the planning constraints that are further restricting growth at the Airport and specifically recent delays to the Apron 5H project, which is symptomatic of an increasingly difficult planning environment. ✂ [redacted].

4.4 The latest on the north runway is that the procurement process will complete later this year followed by a contract award before the main construction element gets under way early next year. This timeframe would mean that the new runway would not be fully operational until 2022 at the earliest but could be subject to further delays unknown at this time.

4.3 The relevance of Irish GDP growth

4.5 There is also an important consideration surrounding the GDP multiplier which has been used by the Commission in the past. There have been well publicised issues with GDP over the course of this Determination and with a question over the reliability of this metric, the Central Statistics Office ('CSO') have explored suitable alternatives.

4.6 We do not have an issue with the Commission's view that there is a positive relationship between per capita income and the propensity to travel but wish to make the point that our increasingly diverse passenger mix is not necessarily aligned to Irish GDP. We would therefore recommend that any related GDP time series analysis would simply be one of many decision-making tools at the disposal of the Commission and that other related aspects set out within this chapter are considered simultaneously. Ultimately Irish GDP proved to be an unreliable multiplier in the 2014 Determination and the likelihood that this will prove to be the case again in the 2019 Determination, albeit by overlooking the downside risks on this occasion.

4.7 Given that long term reliable forecasts are unlikely to be available for Gross National Product ('GNP') and Gross National Income ('GNI') it might be worth while checking the historical reliability of GDP forecasts from the IMF and OECD in a similar manner to the cross reference between 2014 passenger projections with outturns. This is likely to demonstrate that – leaving aside the question of whether the indicator is a reliable predictor of passenger growth – the likelihood of these long-term projections having such a wide margin of error. This point alone undermines a target being set solely on the basis of an Irish GDP multiplier.

Figure 1: Economic Activity Components that Affect Air Travel Demand

Source: Mott MacDonald / European Commission

4.8 In this regard it is worth noting the relevant economic activity components that affect air travel demand, according to a recent document published by the European Commission[4] and illustrated in the figure below.

4.9 Ultimately, we don't believe that the burden of proof should lie solely with Dublin Airport but we are happy to inform this process via the consultation that will take place in July 2018 and are of the view that GDP projections should be one of many components considered by the Commission.

4.4 Brexit and other relevant developments in the UK

4.10 The Commission is right to state that the outcome of Brexit remains unknown in addition to the conditions for the transition period and the potential implications for Dublin Airport's traffic forecast. We will be cognisant of developments in this space in advance of submitting our regulatory proposition.

4.11 A key consideration in this regard is the approach taken by the UK's Civil Aviation Authority ('CAA') who is also considering the impact that Brexit will have on traffic growth at UK airports. Their response has been to project growth of approximately 2% (CAGR) which is well below what an Irish GDP multiplier would infer.

4.12 With our traffic significantly exposed to UK traffic and the UK environment in general, it is important to consider that our growth to that region is stagnant and out of kilter with other key regions. It is therefore not beyond the realms of possibility that Brexit will act as a significant additional drag on passenger growth at Dublin Airport, beyond the 32 million passengers per annum in 2019, which underpinned the PACE consultation process.

4.5 Operational disruption

4.13 In the context of passenger targets, an important consideration by the Commission is the scale of the Capital Investment required and how the resulting operational disruption may act as a short-term constraint on capacity. For example, in the current CIP projects, such as apron and taxiway rehabilitation has resulted in stands being closed and therefore unavailable at key times.

[4] Page 22
https://ec.europa.eu/transport/sites/transport/files/2016_eu_air_transport_industry_analyses_report.pdf

4.14 Other such projects that have resulted in stand closures include:

- Installation of Hydrant Fuelling
- Stand Realignment Projects
- Introduction of AVDGS
- Introduction of FEGP
- Installation and/or repair/upgrade of jet bridges
- New line markings requiring painting of new lines/hammerheads

4.15 There is also the important issue of upgrading Terminal 1 to Standard 3 Hold Baggage Screening, which is unlikely to be completed until post-2020. We will endeavour to avoid any operational disruption but this coupled with the absence of a derogation from the Irish Aviation Authority ('IAA') it is a risk nonetheless.

4.6 Alignment between passenger targets and CIP requirements

4.16 We do not agree with the Commission that the passenger target and CIP requirements need to be neatly aligned. It is important to consider recent events whereby airlines did not support necessary investment in 2014 but subsequently publicly criticised daa for failing to sufficiently invest in infrastructure. In other words, in the incentive based regulatory framework, we should be incentivised to continue to beat the targets set for us and in the event that we are successful there should be adequate infrastructure in place.

4.17 Despite the relative success of the Supplementary Capital Expenditure Programme in 2017 and 2018, interested parties will be aware (with Aer Lingus suggesting in its submission to the Commission) that in hindsight it was insufficient – in other words, there should be sufficient headroom for infrastructure requirements. This approach has the added benefit of maintaining service quality.

4.18 The Supplementary Capital Expenditure Programme resulted in fast-tracked projects not receiving an allowance for the full amount of expenditure required to progress infrastructure that airlines supported. Moreover, this process lasted for approximately 18 months and resulted in important projects being delayed accordingly, with some experiencing further planning delays once progressed (e.g. Apron 5H).

4.19 While we welcome the possibility of a Supplementary Capital Expenditure Programme going forward, it is quite a lengthy exercise from start to finish as Dublin Airport is required to undertake extensive engagement with airport users before submitting to

the Commission and subsequently responding to the Commission's consultation and draft decision.

4.7 Volume Risk Allocation

4.20 The allocation of volume risk to Dublin Airport in the existing Determination has resulted in financial benefits due to higher passenger traffic growth compared to forecasts. It is important however to recall that this has not always been the case and that approximately a decade ago, we bore the brunt of taking on this volume risk when passenger traffic experienced a considerable shock. The direct loss to Dublin Airport due to an unachievable target of passengers for the 2010-2012 period was €36 million[5].

4.21 A key concern of ours is that our ability to outperform in one Determination will adversely influence the target following a reset in a subsequent Determination. From the capacity constraints and other constraints identified above it is clear that there will be limited scope to financially outperform in the next Determination following a reset in 2020. We have already committed to providing the Commission with our 'latest expected' mid-2019, which will ensure the base year in 2020 is as accurate as possible, thereby lending itself to a more reliable reset compared to in 2015.

4.22 Furthermore, the Airport is incentivised by the Commission to exceed the target for passenger growth. It would be counterintuitive and counterproductive if a such a desired behavioural response was to adversely affect an ability to continue to outperform in future periods.

4.23 ✂[redacted].

4.8 Dublin Airport's consultation on passenger projection methodology

4.24 The Commission correctly notes that our intention was to hold this consultation in Q2 (i.e. June) but we have decided to hold off until the date has passed for submitting responses to the Issues Paper, particularly as there will be further consultations with the same stakeholders on Terminal 1 Hold Baggage Screening during this time.

[5] See Page 7 http://www.aviationreg.ie/_fileupload/2013-09-30%20DAA%20Response%20to%20IP.pdf

4.25 This will represent an opportunity for both the Commission and Airport Users to demonstrate what is perceived to be the most appropriate approach to forecasting traffic over 2018-2024. There will also be an opportunity for stakeholders to provide their latest traffic projections to Dublin Airport on a confidential or non-confidential basis.

4.9 Summary

4.26 In summary, this section sets out some key preliminary issues that the Commission should consider when setting the passenger target at Dublin Airport. Many of these issues fuelling considerable uncertainty are variable by their nature and should be closely considered by the Commission over the next 12-15 months.

4.27 It is also unlikely that the Commission will be in a position to set a passenger target using a fully disaggregated approach as airport users are unlikely to be in a position to submit reliable medium-term plans. It is also clear that such a simplistic aggregated approach would inevitably overlook material considerations and result in a passenger growth target that is too aggressive.

4.28 Assuming that the Commission is willing to consider the points raised within this chapter and the outcome of our consultation, we would be willing to continue with the status quo whereby the Airport takes on the volume risk following the resetting of the passenger target.

4.29 While demand is expected to be strong but capacity likely to be somewhat restricted, the following indicators need to be factored into account when the Commission is setting its targets:

- ✂[redacted];
- Operational impacts arising from the CIP;
- Possible downside risks from Brexit (e.g. treatment of UK from security perspective);
- Employment trends;
- Trends in oil prices;
- Consumer confidence.

4.30 In this regard, we request that the Commission does not simply consider a demand forecast but also differentiates between a capacity constrained forecast before setting its target. Ongoing developments from the Slot Coordination Committee are relevant in this regard.

5. Operating Expenditure

5.1 Overview of Operating Expenditure ('Opex') Building Block

5.1 The Commission notes in paragraph 6.2 of the Issues Paper consultation that its objective is to set Opex targets which are challenging, yet achievable. Consistent with other building blocks, Dublin Airport is of the view that we should be incentivised to beat the targets set by the Commission. We are of the view that this is not possible given the Commission's previous views on what represents efficient pay and non-pay operating costs, and would welcome evidence based reasoning from the Commission on how it could have been achieved without adversely impacting on passenger welfare.

5.2 This is clearly demonstrated by comparing the existing Opex allowance set by the Commission with the incurred spend that is necessary to run the Airport and maintain a good level of service quality. It is our view that the Commission applied unrealistically low elasticises for staff areas. Notwithstanding this point, we appreciate the asymmetries of information that the Commission faces when setting these targets and would like the Commission to acknowledge how it proposes to deal with the asymmetries specifically relating to Opex.

5.3 Consequently, we are requesting that as part of its bottom up assessment, the Commission recognises realistic cost drivers and is not simply guided by percentage changes in all circumstances. For example, all Central Functions areas were assigned no elasticity, which is completely at odds with the reality. As the business has grown, it has required more support services such as Procurement, Legal, Shared Services etc.

5.4 The Commission notes that we have discretion to spend on Opex as we see fit and that the Commission only assesses compliance with the overall price cap. It is not clear what the purpose of this statement is nor why it would be necessary to monitor compliance on operating expenditures once an aggressive, unrealistic target has been put in place on an ex ante basis. In other words, providing the Airport with an Opex target that is so difficult to achieve implies that the only way the Airport can be remunerated for efficient Opex spend is via a financial outperformance on another regulatory building block. A somewhat related point is that such a target is only effective to the extent that it minimises cost overruns compared to the allowance itself – there is no doubt that the Commission could achieve the desired effect by recognising the need for a higher Opex allowance.

5.5 Given the challenges that accompanied the unexpected passenger growth, we have been monitoring our Opex per passenger against CAR's implied Opex per passenger allowance. On this basis, we note that we have achieved a better Opex per passenger ratio in the first part of this Determination period when compared to the targets set by the Commission, and have realised an Opex per passenger ratio in 2017 just above the target. So whilst in absolute levels, we have incurred higher Opex than had been envisaged, the Opex activities for delivering a service on a per passenger basis has been relatively in line with expectations.

5.6 Following on from the previous points and in conjunction with the Commission's "*assumed inelastic response of Opex to passenger numbers*" we believe that Opex should not only be considered from the perspective of passenger volumes but also from a service quality perspective, which appears to have been largely overlooked in the Opex section of the Issues Paper consultation. In paragraphs 4.7-4.8 the Commission has acknowledged the increasingly diverse passenger profile, which is driven by five-star airlines including two new direct Asian routes in June 2018 in addition to the expanding transfer model. Arising from this is an associated Opex costs to ensure every profile of passenger experiences an acceptable quality of service.

5.2 Opex drivers and elasticities

5.7 Dublin Airport welcomes the list of possible explanations provided by the Commission in paragraph 6.8 of the Issues Paper and in doing so recognises that the level of unexpected change in passenger numbers might have prevented our ability to deliver efficiencies. We are of the view that the Opex elasticity assumptions were unrealistically low and that the increase in scale occurred at such a pace that inhibited what would otherwise have been an efficient response.

5.8 It is possible to delve further into these possible explanations provided by the Commission by examining new lines of Opex and other unforeseen trends, each of which are discussed later in this Section.

5.9 The Commission is seeking views from respondents on the explanation of the difference between projected and outturn Opex. However, it is important to note firstly that our view of projected Opex in 2013-2014 differed significantly from the view taken by the Commission and its consultants SDG at the time. Secondly, it is important to frame this question in the context of how the Commission has forecast Opex i.e. it engaged SDG to assess the most efficient prospective Opex costs of an unconstrained Airport operator. Therefore, our position is that it is not entirely

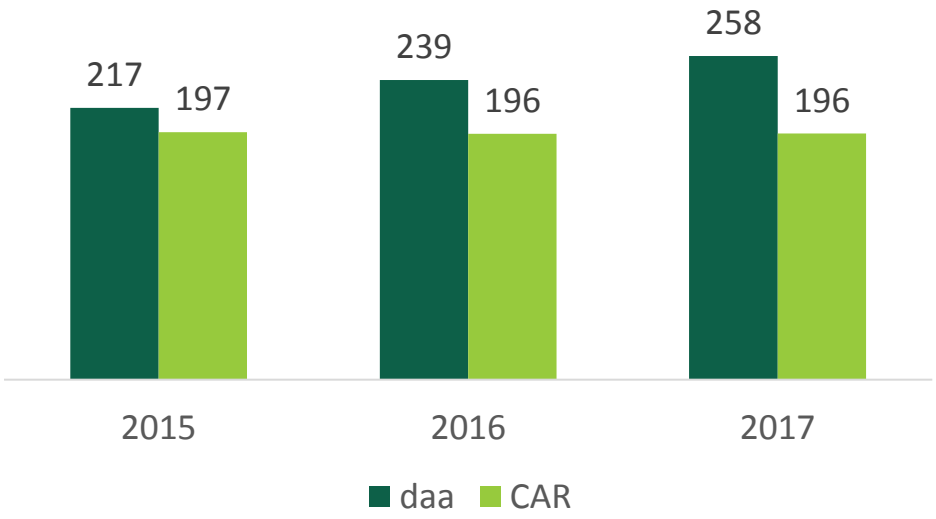
surprising that the Commission's forecast (or target) for Opex has been different to outturn Opex.

5.10 Further to the Commission's request for evidence in paragraph 6.13 of its Issues Paper, we have listed the relevant factors below and intend to provide more detail in our Regulatory Proposition.

5.3 Variance in actual Opex incurred with the Commission's target

5.11 In the period 2015-2017 annual operating expenditure incurred at Dublin Airport has exceeded the allowance set out in the 2014 Determination and this deficit is expected to continue in 2018 and 2019.

Figure 2: Dublin Airport actual Opex (€m) 2015-2017 versus CAR Opex target (€m)



5.12 Beyond the disagreement on the appropriate baseline and relevant elasticities, there are a number of more specific and relevant factors contributing to the divergence, as set out below.

5.13 We agree with the Commission (paragraph 6.8 of its Issues Paper) that the elasticity assumptions were inappropriate for the current Determination period. Consequently, we are of the view that the Commission should be willing to explore the need for new assumptions. We disagreed with the Commission's elasticity assumptions in the 2014 Determination which were understated on a category by category basis. For example, the Commission assumed 'Facilities & Cleaning' had no volume elasticity and rather it was based on the size of the space, while this is one element i.e. the fixed cost, there is also a volume element. Moreover, the busier the airport, the higher utilisation of the space which requires more frequent cleaning, supplies etc. The Commission's

elasticity assumptions by category resulted in a 0.16% increase in Opex when there was a 1% increase in passengers, which was significantly understated in our view.

5.14 Looking at the change in costs over the period 2014-2017 and adjusting for price changes, capital infrastructure, compliance effects etc., we see similar volume elasticities that were implied by independent consultants Booz in the 2014 Determination. The volume impact on Opex accounts for c30% of the overall Opex increase experienced to date. Revised elasticities need careful consideration and adjustment in the forthcoming determination to ensure Dublin Airport is granted an efficient Opex allowance for the relevant passenger target.

5.15 We wish to respond to the Commission's view in paragraph 6.10 of the Issues Paper as it is important to emphasise that 'Other Materials and Services' includes direct costs for operating commercial business such as Executive Lounges and Platinum Services which are volume driven and offset by higher commercial revenues. High level estimates show the increase in staff costs to date is c50% price driven (through contractual pay agreements) and c30% volume driven.

5.16 The remainder is driven by compliance, infrastructure and new business. Only changes in the consumer price index have been allowed for in the price cap when annual pay inflation has trended significantly ahead. Additionally, contractual pay agreement with unions have impacted annual staff costs along with other changes such as the new employer defined contribution pension scheme.

5.4 Factors driving the divergence: distortionary effect from previous efficiencies

5.17 It would appear to us that efficiency gains achieved over the period 2010-2014 have had a distortionary effect on the target set by the Commission back in 2014. Following the publication of the 2009 Determination, we faced a substantial financial gap between our cost projections and the Commission's Opex allowance. In order to rectify this, we embarked on a major cost recovery programme which resulted in significant payroll reductions and further non-payroll cost reductions that were realised through savings in repairs and maintenance, energy, insurance and professional services.

5.18 The following table sets out the specific details of the cost savings over the period 2010-2012, as set out in our 2014 Regulatory Proposition.

Table 2: Outcome of DAA Cost Recovery Programme

	€m	€m
CAR Target savings		-29.0
Existing facilities Payroll savings	41	
Existing facilities Non-pay savings	9.5	
T2 Payroll savings	6.3	
T2 Non-pay savings	8.4	
Total DAA savings		65.7
Cost Inflation above CAR Assumptions		-5.4
Net Opex position 2012		31.3

5.19 The success and extent of the cost reductions to our cost base can be attributed to the timing and unique set of circumstances that prevailed. It also occurred during a time in which passenger growth was under significant pressure. While the benefit of these savings has remained within our cost base since 2014, it was not possible to repeat the same level of savings in this Determination period and particularly in light of such strong passenger growth.

5.5 Factors driving the divergence: new infrastructure

5.20 Furthermore, the significant increase in airport traffic (both in passenger and aircraft volumes) placed an elevated strain on airport infrastructure, with certain facilities nearing or already operating at maximum capacity throughout 2017. The table below illustrates the findings of Dublin Airport's 2017 capacity assessment.

Table 3: Summary of Dublin Airport's 2017 capacity assessment

Facilities operating at:	Departure Processors	Arrival Processors
Maximum Capacity	• Airport Access Roadways • Car Parking • Aircraft Parking Stands • Apron & Taxiway System • Runway	• Runway • Apron & Taxiway System • Aircraft Parking Stands • Immigration (T1) • Car Parking • Airport Access Roadways
Emerging Capacity Constraints	• Kerbside Parking (T1) • Check-in (T2) • Baggage System (T1) • Transfer Facilities • US Preclearance • Retail/Wait for Gate/Food and Beverage • Departure Gates • Ground Equipment Parking	• Ground Equipment Parking • Baggage Reclaim (T1) • Kerbside Parking (T1)
Capacity Surplus Exists	• On Airport Roadways • Kerbside (T2) • Check-in (T1) • Baggage System (T2) • Central Security*	• Immigration(T2) • Baggage Reclaim (T2) • Arrivals Halls • Kerbside (T2) • On Airport Roadways

* New procedures at Security for S18 have resulted in a revised processing rate which should turn it to amber

5.21 Given the capacity shortages, short-term operational based solutions were required in order to meet airport user requirements and maintain quality of service. However, these short-term solutions contributed to additional operating costs and diseconomies of scale. This trend will continue into the next Determination and one that CAR and its cost consultants should reflect in their target.

5.22 New infrastructure has been put in place since 2014 that hadn't been wholly envisaged in the 2014 Determination from an Opex perspective, including:

a) Pier 1 Extension,
b) PBZ / South Gates,
c) Pier 2 Segregation
d) South Apron Stands Phase 1
e) Car Park i.e. T2 Multi-storey Car Park with four floors and a total of 1,402 additional spaces

5.23 Associated Opex costs incurred by Dublin Airport and without remuneration include:

a) Cleaning
b) Maintenance
c) Rates
d) Bussing in addition to staffing costs associated with vehicle escorting
e) Security

5.6 Factors driving the divergence: necessary step changes

5.24 Over the period 2015-2017, there have been a number of step changes in our Opex related to additional airport infrastructure (e.g. bussing to satellite stands), security costs and labour rates (e.g. pay restoration as per the contractual terms of the CRP Agreement from 2010[6]), with this latter point detailed below. Demand for labour has increased in the Irish economy driving up average labour costs, this trend has been reflected in rising payroll costs at Dublin Airport which increased at a marginally slower rate than the national average. Similarly, the Commission should examine the rate of pay compared to other unionised environments and whether or not these other environments focus on productivity agreements.

5.25 It is also the case that we were required to fulfil a number of obligations relating to pay restoration and union wage agreements. Going forward Dublin Airport will have obligations in relation to wage agreements and further contractual pay increments which will increase our operating cost base and we would recommend that these are included in the Commission's operating cost allowance. We are cognisant that the Commission has expressly taken a different view in previous years but are of the view that this issue warrants further consideration. We return to this issue of contractual arrangements in Section 5.15 below.

5.26 Understandably, the Commission did not envisage the complete change in economic circumstances in Ireland, in which the economy has experienced a transformation going from high unemployment to almost full employment. This has not only had an impact on our direct payroll costs that are subject to pay inflation but many of our non-pay costs have also been subject to the rising payroll costs of our suppliers.

[6] At the start of the Determination period the Commission does not appear to have believed that restoration would take place in this Determination period (given the assessment of passenger prospects) and so did not make an allowance, whereas we had identified this as a major risk.

5.7 Factors driving the divergence: necessary compliance related

5.27 Since 2014, Dublin Airport has incurred additional compliance costs attributable to Airside Health & Safety, Security Training, HBS and Insurance. These additional costs have amounted to more than €5m per annum to date and they are currently not remunerated under the price cap.

5.8 Factors driving new Opex in the current Determination period and beyond

5.28 There are a number of additional new lines of operating cost that will form part of our operating cost base going forward and these need to be considered in the next Opex allowance. These include, but are not limited to, the following:

a) Investment in people and HR initiatives with increased investment in training, more employer staff engagement and greater investment in the employee experience;

b) Increasing insurance bill with regard to greater security threat plus increasing public/employer liability costs;

c) Increased litigation culture within procurement e.g. cost of defending/settling claims etc.

d) Increased IT costs related to Cloud costs for HR information systems;

e) Increased costs relating to our aim of becoming carbon neutral.

5.29 In the interest of providing further context, we have expanded on one of the relevant new lines listed above – the goal to become carbon neutral – and will provide more comprehensive information on all of these aspects in our regulatory proposition.

5.30 As part of its strategy Dublin Airport is aiming to be a carbon neutral airport by 2020 and to achieve a number of specifc sustainability targets by 2024. ACI Europe has committed to 100 European airports achieving carbon neutrality by 2030 - many of our peer airports have either already achieved (133 European airports) this or are committed to becoming carbon neutrality. The map below identities airports that are currently carbon neutral.

5.31 In order to become carbon neutral Dublin Airport will be required to impement the following:

- A year on year reduction in carbon emissions (taken on a three-year rolling average);
- Offset the remainder of emissions through purchasing carbon offsets (and green electricity);

- Lead a stakeholder management plan to engage airport stakeholders to reduce their carbon emissions.

Figure 3: Carbon Neutral Certified Airports by Region

Source: ACI

5.32 We are committed to implementing the following sustainability goals

- Achieve minimum compliance for all environmental aspects.
- Advance beyond compliance with respect to all environmental aspects to join peers and/or industry leaders.

5.33 However, achieving the airport's sustainablity goals will involve the implementation of a number of different policy considerations across Dublin Airport campus, including:

- Surface Water Management Policy
- Sustainable Procurement Policy
- Local Exhaust Ventilation Policies (daa fleet/Public bus/Taxi)
- FEGP Policy
- IS399 (Sustainable buildings) Policy
- Waste Management Policies
- Surface Transport Policy
- Staff Training (i.e. new security certification requirements enforced by IAA)
- Sustainable Project Evaluation Policy

5.9 Recognition of regulatory risk (e.g. unforeseen mandated costs)

5.34 We accept that an integral part of the current regulatory model is the risk that actual operating costs for Dublin Airport will exceed the cost allowance set by the Commission. We have accepted this risk on the basis that if Dublin Airport can beat the operating cost target set by the Commission then the company will get to benefit from this cost saving. However, we are concerned that there may be instances where unanticipated costs will be incurred by Dublin Airport as a result of mandated operational requirements in the field of security and compliance which are outside the airport's control and which are not automatically remunerated through airport charges. Such costs should be recognised by the Commission as they are beyond our control and incompatible with incentive regulation.

5.35 Another relevant example of this would be Hold Baggage Screening costs, whereby in March 2017, Dublin Airport's security function became responsible for the provision of Hold Baggage Screening (HBS) at the airport. This was as a result of the transfer across the State of responsibility for this service from airlines to airport operators, by way of amendment to the National Civil Aviation Security Programme ("NCASP"). These incremental costs have come on stream from 2018 and are estimated to cost Dublin Airport almost €5m up until the regulatory reset. If these costs occurred earlier in the regulatory period, the incremental unfunded costs would be substantially higher. Both incremental cost items are efficiently incurred expenditure and mandatory costs outside the control of the airport which should be remunerated aligned with economic principles.

5.36 Prior to this, while we were the provider of HBS infrastructure, airlines operating at Dublin Airport had direct responsibility for the provision of this service and they outsourced the provision of this function to third party providers. These HBS costs are currently not included in the operating expenditure allowance set out in the 2014 Determination, therefore for the duration of this current regulatory period, Dublin Airport is not being remunerated for these necessary and efficient costs.

5.37 We believe that instances such as this represent an unacceptable level of regulatory risk which should be addressed by a cost adjustment mechanism that would be compatible with incentive regulation. We would therefore recommend the introduction of an additional annualised cost allowance that would allow for the recovery of efficient costs that are incurred by Dublin Airport over the course of the regulatory period but which were not anticipated in the Commission's operating cost allowance.

5.38 The Commission is aware of the above issues and we are willing to engage with the Commission regarding an appropriate mechanism for recognising such costs. However, we are not in favour of a 50/50 risk sharing mechanism as this can unnecessarily result in significant financial exposure.

5.39 One option would be to provide a risk-sharing mechanism for regulatory, compliance or costs fully outside of our control and which are material in nature on an annual basis e.g. costs greater than €0.5m p.a. A regulatory formula adjustment for the inclusion of incremental costs outside the control of the airport would be the best method for adjustment. A delay in remuneration until the subsequent regulatory determination must take into account time value of money adjustments as the impact of receiving the remuneration some 5 years on has a cost to the airport.

5.10 Approach to Setting the Operating Cost Allowance

5.40 In paragraph 6.23 of the Issues Paper, the Commission has sought views on an appropriate methodology for arriving at a figure for the Opex allowances. We are firmly of the view that the following factors must be considered:

- An efficient Opex baseline
- Volume elasticities which require a more granular review by cost category
- Infrastructure impacts
- Known price changes outside of CPI e.g. Fingal County Council rates revaluation

5.41 Underestimated elasticities have a significant impact on Opex costs. As demonstrated by the Commission, the 2014 Determination model would expect c€6m of additional costs in 2016 vs 2014 due to volume (15%). However, we calculate that of the €41m increase in costs, approx. 35% is due to volume. Pay restoration has been a significant factor behind this divergence.

5.42 In relation to benchmarking it is essential that the Commission considers specific business Opex not present at benchmarked airports such as CBP or specific infrastructure requirements e.g. South Gates. More information on appropriate benchmarking is provided below.

5.11 Importance of appropriate comparators

5.43 We agree that top-down analyses such as indirect and direct benchmarking can be useful for drawing high level comparisons (but only up to a point given the well-known limitations in such international benchmarking) and in highlighting specific areas for further bottom-up consideration. In direct top-down analyses, Dublin Airport can be

compared with its peer airports across a number of partial productivity measures. However, in order for these comparisons to be meaningful they must at a minimum be based on the following:

- the comparator airports which are used must be only peer airports of a similar size;
- the chosen comparator airports must be operating in a broadly similar business environment;
- data related to the selected comparator airports must be normalised as far as possible to take account of any significant airport/industry differences in the direct benchmarks;
- comparisons must take account of the fact that airports can have a different physical architecture driving their cost base, airports tend to exhibit economies of scale and that different airports can provide different levels of service quality and this will be reflected in cost differentials between the airports.

5.44 Therefore, choosing an appropriate set of peer airports and making the above adjustments are essential if top down benchmarks are to be used to compare relative operating efficiency. However, any benchmark should only be used in parallel to bottom up/ airport specific reviews – benchmarks are complementary only.

5.45 The following airports could be considered as possible comparable peers for Dublin Airport based on their relative size, their traffic mix and their customer base. All of these airports have crossed the 25 million passengers per annum threshold[7].

Zurich	Lisbon	Copenhagen	Munich
Manchester	Gatwick	Stansted	Barcelona
Oslo	Paris Orly	Rome	

5.46 In addition, it is also possible to look at indirect benchmarks where Dublin Airport can be compared to other sectors in the economy or the economy as a whole for variables such as productivity and costs. These measures may provide interesting high-level comparisons however care needs to be taken that the indirect benchmarks are based on like for like comparisons where they take account of the unique characteristics of the airport sector and adjust for relative differences in capital intensities and technology.

[7] Providing of course the relevant data is available with good explanation of how the cost categories are compiled.

5.12 Inextricable link between Opex and Service Quality

5.47 We have addressed the important issue of linking quality of service with Opex targets in Section 10. Ultimately however we believe the burden of proof in this regard should not be solely placed upon Dublin Airport and that the Commission should examine relevant precedent and propose innovative ways of considering this very important issue that directly impacts the airport user and passenger experience.

5.13 Staff efficiencies

5.48 The Commission asks in its question 8 if efficiencies are identified, how long should Dublin Airport have to achieve them? We understand this question to be primarily in the context of paragraph 6.53 and 6.36 of its Issues Paper consultation.

5.49 Both energy and telecoms regulators in the UK have recognised that regulated firms have to incur transformation costs, which are inclusive of redundancy costs, and include an allowance in regulated price settlements.

5.50 In energy in the UK, redundancy costs are allowed in a total expenditure approach (totex) for the current control of the electricity distribution companies[8]. Ofgem also makes a cost allowance for "workforce renewal". This allowance is given to the networks to do the necessary training/upskilling that is required to refresh an ageing workforce, many of whom are coming close to retirement[9].

5.51 In telecoms, Ofcom allowed restructuring costs which included redundancy costs in both the WLA Control (2018) and LLU and WLR Charge Control (2012)[10].

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[8] The term used is 'atypicals – severance' and is defined as: "Payments made to secure the exit from the business of an individual, excluding any Early Retirement Deficit Contributions (ERDCs)." Appendix 2: RIIO-ED1 Electricity Distribution Price Control – RIGs : Version 4.0. See Glossary page 32 – heading Atypicals - Atypicals Non Severe Weather in Totex in Price Control.

[9] https://www.ofgem.gov.uk/sites/default/files/docs/2014/11/riio-ed1_final_determination_expenditure_assessment_0.pdf Page 128/129. Renewal costs are wrapped up into a single aggregate cost category called "closely associated indirects".

[10] https://www.ofcom.org.uk/__data/assets/pdf_file/0023/112487/wla-statement-vol-2.pdf page 61, footnote 133; Restructuring costs relate to changes in BT's organisational structure that result in redundancy payments and property rationalisation provision costs relate to BT's strategy of consolidating its office space to enable the mothballing and subletting of buildings. Ofcom used an average cost for this cost category in the base year, which are then forecast forward.

https://www.ofcom.org.uk/__data/assets/pdf_file/0018/50355/annexesmarch12.pdf page 62, paragraph A3.80. Ofgem explicitly says that to achieve efficiency gains, some redundancy costs need

5.52 These decisions are consistent with a recognition that previous decisions were efficient and should be respected, but that circumstances have changed which are outside management control due to changes in business circumstances. We believe that this point is especially relevant in the context of the Commission's paragraph 6.36 where it has reminded stakeholders of a finding by the appeals panel in 2009.

5.14 Rolling Incentive Schemes

5.53 The scheme operates by 'rolling-forward' the value of any savings first made in years two, three, four and five into the next regulatory period such that the value of such savings would be retained for the equivalent of five full years before pass through. Under this scheme Dublin Airport is to enjoy the same benefits whenever in the regulatory cycle it realises a cost saving. The savings to be rolled into the next regulatory determination period would be limited to the saving amount in the final year of the current determination period.

5.54 Given Dublin Airport's outturn OPEX performance since 2015, the airport has not been eligible to benefit under this scheme during the current regulatory determination period. While we support the retention of the rolling incentive scheme, its efficacy will remain questionable unless the Commission recognises the Opex that is being incurred as being efficient. In order for rolling incentive schemes to operate as envisaged by the Commission, the baseline must be aligned with the actual operating model at the start of the Determination. Continued incentivisation is required however and we are open to suggested improvements for incentivising and monitoring.

5.15 Contractual Commitments

5.55 Further to paragraph 6.34 of the Issues Paper in which the Commission has acknowledged the existence of commitments to incremental progression in salary and subsequently set out how these commitments can be viewed, we are of the view that it is imperative that the Commission recognises these developments. We are of the view that these are the costs which are incurred and that we should be remunerated accordingly.

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to be incurred : 'For the purpose of reflecting our efficiency assumption in our cost modelling in the March 2011 Consultation, we applied a gross efficiency assumption of 5.0% (i.e.' 0.5% higher than the net rate) and *included the increased leaver payments that we estimated would be incurred to achieve this saving*. The aggregate effect was similar to a net efficiency assumption of 4.5%.'

5.56 We do not agree with the simplified view that we chose to enter into such contracts and that efficiency targets should be set independently as this could result in Dublin Airport incurring necessary expenditure to operate but the Commission is suggesting we should not have entered into such contracts.

5.57 In this regard it is important to recognise recent decisions from the Workplace Relations Commission ('WRC') including one involving Aer Lingus that preceded an important deal that we made. While such decisions are not legally binding there is a strong possibility that some form of industrial action would follow if we were to reject the findings.

5.58 It is also important to emphasise that our growth in pay is not out of kilter with other unionised industries in Ireland and we intend to provide comprehensive information on this in our Regulatory Proposition. The Commission should recognise that our deals frequently contain productivity commitments which is not always the case in other such environment.

5.59 Since 2015 Dublin Airport has been required to fulfil a number of obligations relating to pay and salaries for employees. These include the following

5.60 Pay increases relating to salary increments:

- Dublin Airport frontline employees are on incremental pay scales/bands. Frontline employees receive an annual increase in pay each year until they hit the top of their scale/band.

  ✂ [redacted]

- Employees of daa tend to have increments paid annually in April, this population is a decreasing group of employees.
- Employees of DASL/ASC have performance based increases which are paid in January each year. DASL/ASC employees are where all of our new recruits come into the company.

5.61 Pay Increases relating to Labour Court recommendations:

- On the 26th May 2015, the Labour court recommended a 4.04% cumulative pay agreement (LCR 20997). This related to a number of claims made in respect of the Cost Recovery Plan (CRP). CRP took effect in February 2010, this involved employees taking an average pay cut of 5.5%. The cuts were on a graduated scale whereby the highest earners took the largest cuts in pay.

5.62 Pay increases relating to Cost Recovery Plan (CRP) pay restoration:

- There were specific rules around company performance (PAT or ROE) whereby if the daa Group began hitting agreed targets, the pay cuts would be restored. The daa Group achieved these targets in 2015 and has consistently achieved them since then. Therefore, in 2016, the pay cuts were reversed.

5.63 Pay increases relating to national wage agreements

- There have been no national wage agreements during this time period.

5.64 Pay Increases relating to union agreements / pay claims

- We have recently formalised aggrements with our three largest unions, SIPTU, Forsa and Mandate. This has resulted in the following pay awards:

- Mandate and Forsa
  3-4% from 1 April 2017
  3-4% from 1 April 2018
  3-4% from 1 April 2019 until 31 March 2020.
  ✂[redacted]

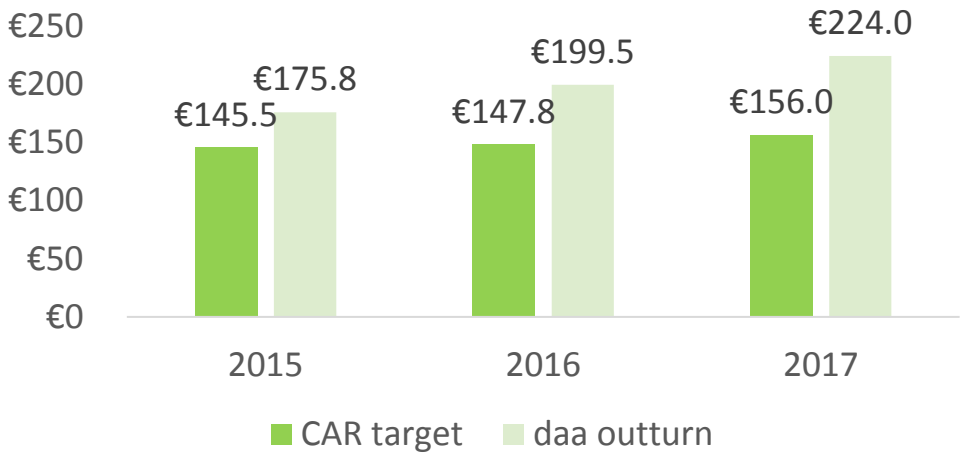
- SIPTU
  3% from 1 April 2017
  2.75% from 1 April 2018
  2.75% from 1 June 2019 to 31 July 2020.
  ✂[redacted]

6. Commercial Revenues

6.1 Commercial targets compared to outturns

6.1 Commercial Revenues exceeded the Commission's target by €68m in 2017, having experienced a compounded annual growth rate of 14% over the period 2014-2017. The increase in commercial revenues from €152m in 2014 to €224m in 2017 was achieved by both volume (i.e. passenger growth: €32m) and price (i.e. yield management etc: €36m) growth.

Figure 4: Actual commercial revenue compared to CAR targets (€m)



*2017 Prices

6.2 It is important to clarify that the outturn elasticities presented in Table 7.3 of the Commission's Issues Paper includes revenue uplifts that were generated from yield initiatives. If one excludes the additional revenue from capacity and price/yield impacts, the relevant elasticity is 0.7.

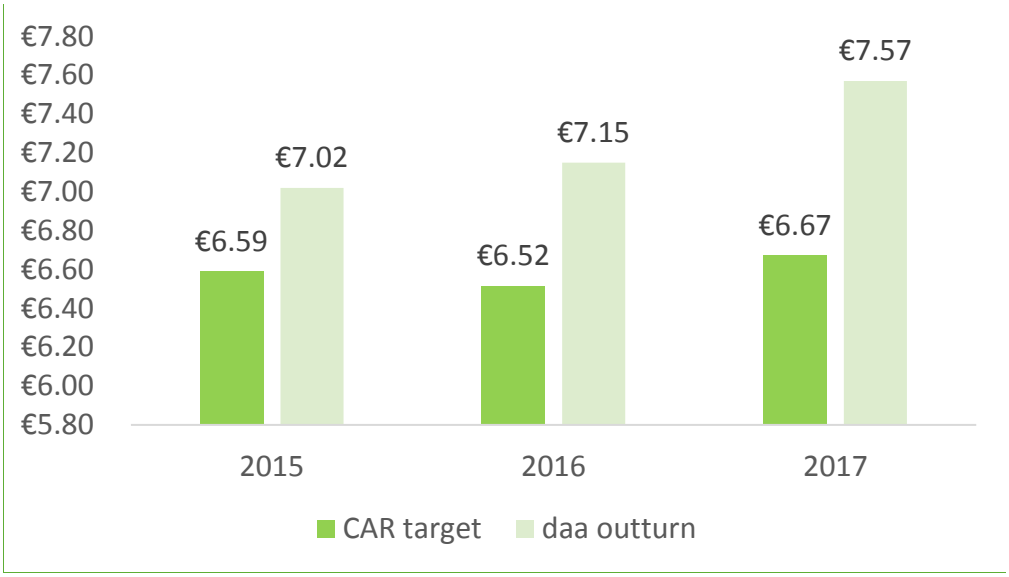
6.3 With 56% of the revenue growth between 2014-17 due to capacity expansion and contract repricing / yield management, the true volume based growth accounted for less than half of total growth in the period at 44%.

6.4 It is important to recognise that the competitiveness of our key revenue generating businesses has increased considerably meaning there is limited scope for such gains going forward.

6.5 With less than half of the out-performance being driven by passengers, it must be recognised that a tipping point exists whereby volume elastic revenue would be incapable of reacting to passenger growth due to capacity constraints and yield management thresholds. The following is relevant in this regard:

- Approximately 20% related to revenue generating capex, and
- Approximately 35% related to yield management and contract renegotiation.

Figure 5: Actual commercial revenue per passenger compared to CAR targets



*2017 Prices

6.2 Setting the target for commercial revenues

6.6 This section responds to paragraph 7.2 of the Issues Paper in which the Commission has invited parties to outline any changes to the econometric approach for forecasting commercial revenues.

6.7 As a general observation, the Commission appears to be open to suggestions on how best to project commercial revenues but has placed a large emphasis on how best it should refine its econometric model. In this regard we recommend that the Commission recognises that the Commercial business unit in Dublin Airport operates on a Profit & Loss basis and it is therefore prudent to review future revenues on the basis of Earnings before Interest, Taxes, Depreciation and Amortisation (EBITDA) as opposed to revenues being completely separated from operating costs.

6.8 We do not agree that evidence from recent years necessarily implies that commercial revenue elasticities are higher than previously thought. There are two problems with the Commission arriving at this conclusion and we have set out our reasoning below.

6.9 Firstly, this does not indicate any change in the long run relationship between passenger growth and commercial revenues. It is possible that if the model were to be re-estimated the elasticity coefficients might increase (simply because the recent experience would contribute to those coefficients). However, if the last few years have behaved somewhat differently to the past we would also expect the standard errors on coefficients to increase. That is the model becomes a less good fit of the data. This means the confidence intervals on any future forecast would be wider. The Commission should take this uncertainly into account when setting overall commercial revenue targets.

6.10 Secondly, measuring the "elasticity" only from the latest period uses a limited reference period from which to compare passenger growth with revenue growth, potentially mixing up correlation and causality. It cannot distinguish between exogenous effects, i.e. the impact of an unexpected surge in passenger numbers on commercial revenues and endogenous effects – our ability to boost commercial revenues in excess of the target in recent years. It would provide very bad incentives if we were penalised for the latter by setting a faster rate of growth on commercial revenues for the next price control.

6.11 Regarding the choice of variables for a refined econometric model, it is difficult to comment on the specific suggestions. This puts a significant burden of proof on the Airport and other stakeholders. Ideally, we would have visibility all variables, ultimately to be based on rigorous econometric testing, which we could then comment on in our response to this consultation.

6.12 Notwithstanding the above shortcomings, we wish to express caution regarding the use of explanatory variables that require forecasting themselves, particularly when these forecasts are uncertain and debateable. This point is similar to what we have raised above in paragraph 4.7 in the context of using a multiplier based on Irish GDP.

6.13 Ultimately we would welcome the inclusion of additional factors in the econometric model but would highlight that there are a number of 'downside factors' not listed in table 7.4 of the Issues Paper (e.g. capacity constraints and yield management thresholds). There may be increased accuracy from adjusting elasticity calculations to reflect capabilities for price and yield management in addition to capex.

6.14 With business data demonstrating capacity constraints in the areas of Direct Retail, Car Parking, Car Rental, F&B and Property, it is not appropriate to assume that a similar uplift through pricing can be achieved in the next determination period.

6.3 Interaction with other building blocks

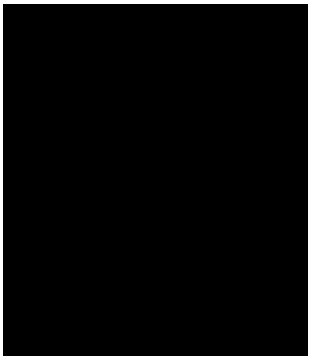
6.15 The Commission will be aware that its commercial revenues target will need to consider the impact of future developments across the campus and how these will impact on our ability to generate commercial revenues.

6.16 While the Capital Investment Programme is still subject to consultation by Dublin Airport and will remain the subject of consultation with the Commission until September 2019, the target will likely reflect the expected capital investment.

6.17 Specifically, a redevelopment of the south apron would displace a significant number of commercial property units and the timing of this redevelopment would have a significant bearing on our commercial revenues target. The Commission would therefore need to align its related capital allowances with the impact it will have on commercial revenues.

6.18 ✂ [redacted].

6.19 ✂ [redacted]:



6.20 ✂ [redacted].

6.21 Conversely, new car parks are required to cater for demand, which will have a positive impact on commercial revenues when completed.

6.4 Risks to commercial revenues (including retail)

6.22 Internationally, retail revenue per passenger is trending down as airports come under pressure from trends in ecommerce and airlines switch their attention to ancillary services. For example, Ryanair has plans to become the 'Amazon of the airline industry', a one-stop shop for travel, selling not just flights, but rooms, transport, restaurant and event bookings and ancillary products such as sun glasses and sun cream'. Ryanair has outlined it ambition to become a global travel retailer, whereby flights become the "bread and milk in the supermarket" and customers data are used to cross sell and upsell other travel related products[11].

6.23 Dublin Airport is not immune to these externalities and this represents yet another reason why past performance with commercial revenues is not the most reliable predictor of future revenues i.e. an extrapolation exercise runs the risk of missing the most relevant variables. Similarly any econometric analysis should include explanatory variables that consider these trends, and the likely impact it will have for Dublin Airport.

6.24 Although Retail has increased since 2014 (up +17%), it is unlikely that similar growth will be achieved again due to the threat of ecommerce (expected to reach 18% - 20% of retail sales globally by 2021) and increased regulation on tobacco and Liquor sales.

6.25 Retail has also been recognised as an area with emerging capacity constraints and regarding components in this category such as Food & Beverage outlets, we are finding that penetration rates for a number of key locations are peaking in May despite passenger volumes not peaking until August.

6.26 A recent S&P report[12] (December 2017) has considered the question of why retail revenue per passenger growth is slowing (see table below). They note that it's the commercial side of the airport business that offers the biggest challenges, owing to the fact that the retail and mobility industries are in deep structural transformation.

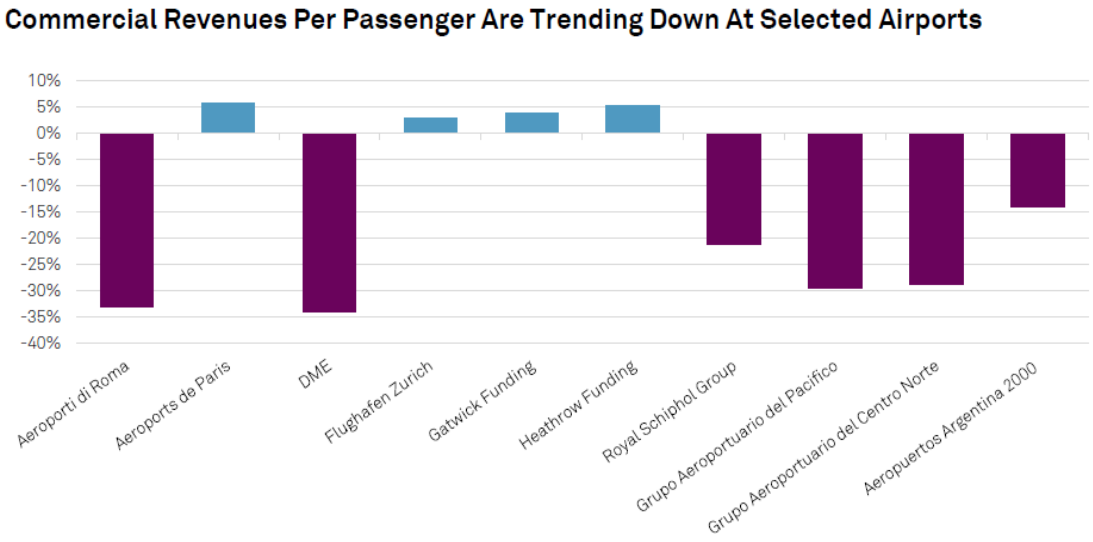
[11] CAPA Airline Leader Summit, Powerscourt, Wicklow, May 2018

[12] https://www.spratings.com/documents/20184/1634005/Are+Airports+Ready+For+Airline%2C+Retail%2C+And+Mobility+Disruption/b12f7329-4eae-423a-aa92-9b3f8fdffdc3

6.27 It notes that after decades of sustained growth, duty-free and travel retail sales contracted in 2015 and were flat in 2016, which may represent a concern given that global tourism during the period was buoyant.

6.28 It further notes that the diverging trends of growing traffic and stalling duty-free and travel retail sales mean that while the underlying travel trends remain positive, passengers can't be counted on to spend as they have in the past.

Figure 6: S&P Global Ratings of Commercial Revenues at Selected Airports



Note: Growth from 2011-2016 (2016 revenues are real figures, adjusted by inflation): Source: S&P Global Ratings.

6.29 This international trend reflects increased online competition and a structural change in consumer preferences away from traditional retail areas. Furthermore, S&P notes that airports are adapting to the pockets of consumer spending where growth is still holding up well, such as eating out or recreational services. S&P concludes this section by noting that if commercial revenues trend down, aeronautical tariffs will need to increase for airports to continue to sustain current margins.

6.30 Separately, S&P explore the impact that mobility trends are having on car parking revenues. It notes that the airport car-parking segment has been going through new challenges in recent periods, facing off airport car parking competition, car sharing, and public transport competition in addition to digital disruption. The effect of car sharing on both airport parking and access has the potential to significantly change airport ground access revenues. Services such as UberX and GoCar provide an increasingly popular alternative to taxis and while car-sharing services obviously compete most directly with taxis, their increasingly popularity may also see more people choosing not to drive to the airport.

6.31 In summary it notes that car sharing may therefore place competitive pressure on airports to provide cheaper car parking services or dedicated waiting areas available where car-sharing drivers can wait for passengers, comparable to existing waiting areas for taxis.

6.32 As per Figure 7 HSBC Global Research has maintained a cautious stance on European airports due to aeronautical and commercial revenue coming under pressure. It notes that unit commercial revenues face challenging mix effects, with luxury retail facing particular challenges.

Figure 7: HSBC Global Research

18 April 2018

HSBC Global Research

European Airports

Cautious stance maintained

EQUITIES
TRANSPORTATION
INFRASTRUCTURE

Europe

- Despite vibrant traffic outlooks, we see listed airport margins facing pressure from fee discounts and weak retail trends

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6.5 Commercial Property

6.33 Commercial Property had 20% vacancy in 2014 and is now operating at <1% vacancy. Looking ahead, revenue is likely to be negatively impacted by up to 25% depending on Masterplan and CIP decisions. For this reason the elasticity of 0 may be too high and we would request that the Commission gives this issue due consideration in its Draft Decision.

6.6 Commercial Concessions

6.34 The majority of the elasticity increase calculated by CAR for this revenue stream relates to the Car Rental contract renegotiation which came into effect in 2017. It is unlikely that such a similar material uplift will be achieved in 2020.

6.35 ✂. [redacted].

6.36 The average transaction value for car rental has increased by less than 1% since 2014, indicating that car rental revenue is purely driven by volume. With capacity an emerging constraint in the car rental business, it is important to address this constraint in order to continue to grow and protect revenues.

6.7 Car Parking

6.37 Car parking is facing significant capacity constraints with average occupancy in 2017 of 88% for short-term parking and 68% for long-term parking. The short-term car park is forecast to hit maximum capacity for eight weeks during the summer of 2018, rendering the business effectively closed during this period. Long-term parking also periodically hits max capacity e.g. week 29 in 2017.

6.38 The increasing frequency and duration of these peak periods is diluting the link between passenger growth and car parking volume growth. Attempts to grow revenue via price increases will likely result in daa losing customers, given the extremely price sensitive nature of the customer base, alternative transport options available, and competition from new car parks near Dublin Airport. In short, price increases have been used as a manner to manage demand but these price hikes have essentially exhausted and there is restricted scope for these to continue.

6.39 With Car Parks operating at peak capacity for two years, demand in peak months has been controlled solely through yield management. For this reason, applying an elasticity based solely on passenger growth is not appropriate as both yield management and capacity are constrained.

6.40 As noted above, there is a point at which even volume elastic revenue ceases to react to pax growth due to capacity constraints and yield management thresholds (the max price that customers will pay before seeking alternatives).

6.8 Advertising

6.41 ✂ [redacted].

6.42 Reducing advertising revenues is in line with the trend in the market: the 'Out of Home' advertising market is down 5% year-on-year in 2017.

6.9 Elasticities

6.43 The Commission note in paragraph 7.9 of the Issues Paper that growing passenger numbers led to an increase rather than a decrease in average revenue per passenger – this is contradictory to what the forecast model predicted and may be an indication that some of the passenger elasticities are too conservative. It further states in paragraph 7.11 that the differences between modelled and implied elasticities are substantial. A possible explanation is that passenger numbers alone cannot capture all relevant drivers of commercial revenues

6.44 This is particularly true in businesses such as Concessions and Commercial Property where revenue is tied to long term rental agreements and 'Guaranteed Minimum Sum' (GMS). Renegotiating these contracts in 2014-2017 created step ups that may not be achievable again in the next determination period. In these businesses, passenger numbers play a minor role. Approximately 90% of the revenue from this category is 'fixed' in nature. The Issues Paper (footnote 26) notes that an elasticity of 0 was applied to the category property concessions – in fact an elasticity of 0 was applied to property rents and 0.2 to property concessions.

6.45 In Car Parks the average revenue per passenger has increased between 2014 and 2017 predominantly through quite aggressive yield management due to capacity constraints (as opposed to passenger volumes). There is a threshold, above which the product is no longer considered to be 'good value for money' and customers seek alternatives. It this context it would not be accurate to assume that revenue per passenger will continue this upward trajectory in car parks without additional capacity.

6.46 As outlined in paragraph 6.25 above, there are similar stories in relation to capacity constraints in other businesses such as Direct Retail and Food & Beverage (where despite pax volumes peaking in August, penetration rates at a number of key F&B locations peak in May - indicating capacity issues in peak months). 2014-2017 data shows that both Property and Advertising are not passenger elastic businesses. Advertising in fact had a negative elasticity when the impact of revenue from the Digital Pods was stripped out.

6.10 Forecasts based on Airports Business Plans

6.47 In paragraph 7.27 of the Issues Paper the Commission notes that '*parties with views on whether alternative approaches should complement or replace the current method based on econometric models are invited to share them*'.

6.48 As noted during the 2014 Determination process, Dublin Airport would welcome the use of the CAA approach (the completion of a detailed review of the various commercial revenue streams) with a 'forward looking' approach. It is understood that this is a more time-consuming exercise complemented by econometric modelling but it is felt that the resulting forecasts would be more accurate and would take account of all factors.

6.11 Benchmarking

6.49 In paragraph 7.37 CAR 'welcome views on whether benchmarks would add to or should replace the current forecasting methodology for commercial revenues'

- Benchmarking should always be used with caution as no two businesses (airports) are the same (different strategies, pax profiles, economies etc.)
- Benchmarks are useful as indicators or to support other analysis but are not appropriate as the main forecast tool.

6.12 Masterplan & CIP Alignment

6.50 It is important that CAR non-aeronautical revenue forecasts take into account Masterplan and CIP decisions.

✂ [redacted].

If that is the case, an elasticity of 0 would not be an appropriate forecast driver.

6.13 Other foreseeable events

6.51 The Commission considers the impact from foreseeable events in paragraphs 7.38-7.43 and is right to consider the possibility of duty free shopping arising from Brexit. We believe that all material considerations, including the risks above, should feed through to a commercial revenues target for Dublin Airport. We would like as much transparency as possible from the Commission in this regard.

6.14 The link between passenger satisfaction and commercial revenue

6.52 ACI has produced a report[13] on whether passenger satisfaction increases non-aeronautical revenues. The research paper is based on the analysis of the ACI ASQ annual global survey carried out at over 300 airports across the world and surveying

[13] http://www.aci.aero/Publications/ACI-Airport-Economics-and-Statistics/Does-passenger-satisfaction-increase-airport-nonaeronautical-revenue-A-comprehensive-assessment-research-report

over 550,000 passengers per year. It is further supported by data generated from the annual ACI Airport Economics Survey.

6.53 This report focuses on high level elasticities relating to non-aeronautical revenues from the perspective of passenger growth and commercial area in addition to how passenger satisfaction can affect growth in non-aeronautical revenues.

6.54 Key findings are as follows:

- An increase of 1% in the number of passengers leads to a growth of Non-Aeronautical Revenue (NAR) ranging from 0.7% to 1%;
- An increase of 1% in the size of the commercial area leads to a growth of NAR of 0.2%;
- An increase of 1% in the global passenger satisfaction mean (as defined in the ASQ Survey) generates, on average, a growth of NAR of 1.5%.

6.55 It follows that a decline in service quality and in turn passenger satisfaction would have a negative effect on commercial revenues. This is an important consideration for the 2019 determination given the recent slipping in the ACI ranking, given the operational disruption that such a substantial Capital Investment Programme will result in and given the capacity constraints that will result in passengers being more inconvenienced that they would otherwise have been.

6.15 Rolling Schemes

6.56 In paragraph 7.57 of the Issues Paper, the Commission asks if it should continue to use rolling schemes to maintain a consistent incentive to realise commercial opportunities throughout the regulatory period. We welcomed the introduction of this mechanism in the existing determination but wish to emphasise that its existence should not adversely influence the target for commercial revenues.

6.57 The Airport's ability to avail of rolling schemes for commercial revenues should not result in any such revenues being implicitly baked into the prospective target set by the Commission in the 2019 Determination. The target should instead be set in an objective manner and be mutually exclusive to our ability to benefit from the rolling incentive scheme.

6.16 US Customs and Border Control (CBP)

6.58 daa provides preclearance for U.S Customs and Border Protection in Terminal 2 and has witnessed strong demand for this service. At present, the CBP facility is nearing full capacity and we are planning to accommodate additional capacity to ensure that future demand can be met without compromising service quality.

6.59 While there is no obligation for daa to provide this optional service, it does boost the attractiveness of Dublin Airport to travellers to and from the US. We do not agree with section 7.50 of the Issues Paper which notes that we are a monopoly provider of preclearance services. The Commission has overlooked the fact that Shannon Airport provides the same service and charges a higher price than Dublin Airport at €10.50 per departing passenger compared to the €7.90 charge per departing passenger in Dublin Airport.

6.60 Moreover, the Commission has overlooked the many issues and risks that accompany the provision of this service and have proved significant enough to prevent other airports from acquiring this service.

6.61 Service quality in CBP is also something that an airline has been disputing for a number of years, noting that the service quality has deteriorated in line with the increase in passenger volumes.

✂ [redacted].

6.62 ✂ [redacted].

7. Capital Expenditure

7.1 Incentives for long term capital investment

7.1 As set out in paragraph 3.1 above, capacity has been under increasing pressure at Dublin Airport and in order to address the issue of capacity constraints both Dublin Airport and the Commission need to consider a more strategic long-term view to airport planning which has been at odds in the past with the more short-term focus of airport users and the medium-term priorities of the regulatory framework.

7.2 The Commission has rightly noted in paragraph 1.7 of its Issues Paper that capital investment has not kept pace with the growth and it further notes that this would suggest that the incentive to make long term investments which have not been part of a regulatory settlement is weak. Consequently, it is essential that the regulatory framework does not continue to impinge on the development of necessary and sustainable infrastructure at Dublin Airport.

7.3 Given the significance of so called weak incentive surrounding long term capital investment, it is imperative that the Commission is transparent about how it intends to rectify this externality. While a supplementary capital expenditure process has no doubt alleviated pressure in the existing Determination, a future Determination should not be the only solution as it is lengthy and can result in further delays.

7.2 Masterplan

7.4 The Commission has recognised the importance of long term planning in paragraph 8.5 of the Issues Paper and states that "*there should then be a clear relationship between shorter term investment plans and the longer term rolling master plan*". The Commission further notes that "*in 2018 [it] will work with Dublin Airport to ensure that users can understand how the five-year plan has been derived from the longer-term plan*".

7.5 As set out in paragraph 3.2 and 3.3 above, the Commission is aware of ongoing developments surrounding the Masterplan and the exertion of countervailing buyer power in this regard. The Commission will also be aware of the time constraints underpinning the regulatory process and the urgent need to deliver capacity post 2020. Consequently, there has been much focus this year on the more medium to long term requirements (out to 40 million passengers per annum) that are compatible with a longer-term strategy (out to 55 million passengers per annum and beyond).

7.6 Furthermore, the Commission will be acutely aware that it is not practical or feasible for Dublin Airport to consult on a wider Masterplan in conjunction with the many other consultations required in advance of our regulatory submission to the Commission later this year.

7.3 50/50 risk sharing mechanism and triggers

7.7 It is our preference to consider alternatives to the general 50/50 risk sharing mechanism for cost recovery, as this can result in Dublin Airport having to absorb efficient expenditure due to necessary changes in scope in projects and other factors out of our control.

7.8 As set out in paragraph 3.22, a good example that demonstrates the magnitude of risk associated with capital allowances is the north runway which received an allowance from the Commission of €247 million in 2014 but is likely to exceed this original estimate by more than €70 million when competitive dialogue completed later this summer. The default 50/50 risk sharing mechanism in place means that the Airport will incur necessary and efficient capital expenditure without a sufficient allowance from the Commission and despite support from stakeholders for this project.

7.9 Furthermore, significant timing issues in capital remuneration cannot be accommodated at larger scales and will depend on financeability at a given point in time.

7.10 It is our view that triggers can sound good in theory but in practice have been very complex and challenging. It is our preference to learn from suboptimal outcomes in the past with respect to triggers in the 2019 Determination

7.4 Early design costs

7.11 The Commission should recognise that as part of the regulatory framework Dublin Airport needs to provide stakeholders with options for developing the campus in order to have a meaningful consultation, and that there are significant costs associated with providing a comprehensive suite of options. These costs are necessary and efficient and Dublin Airport should therefore be remunerated accordingly.

7.12 However, for those options that airport users do not support at the consultation stage and for which there are no allowances provided by the Commission, there is a risk that Dublin Airport cannot be remunerated for these early design costs. We therefore welcome guidance from the Commission in how best these early design costs can be remunerated

7.5 Contingency, escalation and inflation

7.13 The reality of the past number of years is that the allowances received for capital development have included distinct allowances for both contingency and escalation costs but that necessary cost overruns due to factors that have been largely beyond our control have resulted in contingency and escalation costs being insufficient. Furthermore, the ex ante allowances have been subject to general inflation but a much higher construction sector specific inflation has been to the detriment of Dublin Airport. In this regard we acknowledge the Commission's willingness to explore solutions for the 2019 Determination.

7.6 Cost of Capital and CIP related risk

7.14 The Commission should have due regard for the Airport's appropriate cost of capital for over the period 2020-202X as any unjustified reduction in the existing WACC of 5.79% in real terms would be considered by Dublin Airport in taking on the many risks associated with the 2019 Capital Investment Plan.

7.15 We understand that the Commission should not reward the Airport for the same risk in multiple different ways, or by double-counting in other words, but given the magnitude of risk that Dublin Airport faces in the next determination and given the strategic importance of the 2019 Capital Investment Plan for all stakeholders, it is important that the Commission provides clarity on how it will sufficiently remunerate the Airport for risk.

7.7 Recognising risk and setting retrospective capital allowances

7.16 Given the significant shortcomings in the current regulatory framework with respect to capital investment at Dublin Airport, there is a risk that the next capital investment plan will fall short of the mark and negatively affect Dublin Airport, airport users and passengers unless the Commission can address our issues. We therefore explore in this section how the Commission can mitigate risks for Dublin Airport and improve the Capital Investment Process

7.17 The degree to which future costs can be estimated with certainty will differ greatly depending on a number of variables including the planned start date of the project and the level of design. This places considerable risk upon the Airport, which the Commission needs to recognise in the 2019 Determination.

7.18 In paragraphs 8.22 to 8.25 of the Issues Paper the Commission has proposed four options on how it could set efficient capital allowances. We would welcome a view

from the Commission as to what option it considers to be most appropriate, given the greater scope of the next capital investment programme.

7.19 We are of the view that the Gateway approach taken at Heathrow is superior to the existing approach for setting capital allowances. While we currently have a pure ex ante regime in place with a traditional approach to rolling forward the RAB, Heathrow has a light ex-ante regime in which there is more scrutiny by the CAA on an ex post basis in which it also explicitly allows for the recovery of over-spend.

7.20 Compared to the regime currently in place at Dublin Airport, it is more difficult for the CAA in the UK to challenge spending for projects agreed with airlines, which represent market outcomes.

7.21 While the Commission has provided an allowance for capital investment at a group level (currently six groups) with flexibility to allocate expenditure within the respective groups except for those designated as deliverables, the CAA provides Heathrow with an envelope for development projects that is largely based on constructive engagement outcomes[14]. Furthermore, the CAA acknowledges the need to review the allowance required.

7.22 In addition, in the Gateway process at Heathrow, development projects can be identified in advance or during the price control and agreed on a stage by stage basis known as the Gateways. Gateway 3 is the go ahead to proceed with the relevant project and provides the best costing as it is based on the best information, and just in advance of commencing the works. Crucially, this approach reduces the risk of setting a budget well in advance of the project commencing works on the basis of limited information on scope and price. The Gateway approach provides significantly more flexibility.

7.23 The Commission should take note that unlike the supplementary capex process currently in place there is no formal requirement to have a unique set of circumstances to consider a development project mid-determination. Furthermore, the regulator does not need to intervene with its own consultation. Instead, there is an Independent Fund Surveyor - jointly commissioned by Heathrow and the airlines -

[14] Regarding development project capex: The Development Capex Allowance represents an estimate of future capex spending attributable to development projects and is included in the RAB calculation as part of the Q6 settlement. Any differences in the actual capex spend in Q6 will be accounted for through the cumulative development capex adjustment term in the price control formula. http://publicapps.caa.co.uk/docs/33/CAP1151.pdf paragraph 2.47

which plays a role throughout the capital development Gateway Process, advising on project selection, budgeting, implementation and evaluation.

7.24 The Commission's principles for rolling forward the RAB are quite onerous with the burden of proof on Dublin Airport for demonstrating that any overspend was necessary, supported by airlines and efficient.

7.25 Conversely in the UK, the CAA engages in a review of all capital expenditure with the objective of excluding inefficient expenditure. There are clear principles in place that have been agreed by stakeholders, which leads to an objective decision when determining whether specific expenditure was efficient. Of particular relevance is the objective to avoid hindsight bias and there are not any a priory targets regarding how much or how little expenditure the CAA would exclude, with the CAA having the final decision.

7.26 The independent finance surveyor's input is also relied upon as they make impartial records and judgements at the time the decisions were taken as opposed to years after the fact. It also serves to remove potential bias risk of the regulator and has therefore been well received by all stakeholders.

7.27 This process provides airlines with more confidence regarding the governance of capital expenditure. It also leads to more transparency and clarity throughout the process.

7.8 A preferred approach in the 2019 Determination

7.28 While the Commission has not stated its preferred approach in the Issues Paper the Heathrow model appears to be a combination of the options presented by the Commission in paragraphs 8.23 and 8.25 of the Issues Paper. In other words, it would involve setting capital allowances on the basis of an ex post assessment of project delivery and assessing the corporate governance of the framework for capital expenditure.

7.29 In the context of the 2019 Capital Investment Plan, the most important elements of the Gateway process in place at Heathrow is that:

a) An independent fund surveyor is jointly appointed by the airport and the airlines. This minimises the role of the regulator in investment decisions but is not too dissimilar to the current framework where the Commission relies heavily on its independently appointed cost consultants;

b) The costs that are relevant to the RAB are not crystallised until the third stage in the Gateway process and just before construction commences rather than at the time of the price review. Crucially this minimises the risks associated with more simplified design specifications driving future cost estimates and allowances;

c) There is considerable scope for further adjustments to the RAB on an ex post basis following an assessment of outturn costs, which is informed by the judgement of the independent fund assessor.

7.9 Further details on the Gateway Process at Heathrow

7.30 Proposal, planning and approval for *all* capital expenditure goes through a "gateway" process that formalises each of the steps in realising a capital investment. The process is tightly linked with Constructive Engagement and ensures that the appropriate levels of transparency, collaboration and agreement take place at each stage of investment.

7.31 Heathrow needs to justify to the airline community the need for a given project, the options available to pursue and the final budget and delivery plan for investment. At Gateway 3, the critical investment decision (i.e. with the go ahead) is made with the full consensus of the airport and airline community. At this point, stakeholders should have confidence in the expected cost, scope and timeline of the project. Projects that have established strategic need and design may not go ahead once reaching G3, as needs may have changed or the value to airlines has diminished. Plans may be put on hold or altered to achieve agreement instead of passing through to implementation, but all investments must be accepted through this process.

7.32 Subsequent Gateways 4-8 cover the delivery, completion and evaluation stages of each capital project. This includes beginning and finalising of construction, transition to regular operation and ex post reviews of performance and implementation. These stages of capital investment are expected to be undertaken in keeping with the plans agreed during the development stage – the budget, timeline and scope – and are supervised by both the regulator and the airlines. This gateway approach brings clarity and commitment on Heathrow to deliver an investment by an agreed date.

7.33 While comprehensive forecasts of costs and timelines are an important part of the planning and delivery process, these costs are not necessarily binding for the operator. The economic license states that Heathrow is entitled to recover all efficient expenditure on capital investment. Therefore, if cost outturns exceed the budget agreed at G3, Heathrow may still be allowed to include the higher total in the RAB if the regulator deems the additional expenditure efficient.

7.10 Till Exit

7.34 As per paragraph 7.46 of the Issues Paper and specifically with respect to the implementation decisions that the Commission will be making on the till exit in the next Determination, we intend to set out our position in full on this in the Regulatory Proposition. Should the Commission require any information from us in advance of December 2018 we will endeavour to assist.

7.11 Box 2

7.35 Further to paragraph 8.10 in the Issues Paper and the Commission's preliminary view that it intends to include a trigger in the regulatory formulae to appropriately remunerate Box 2 when the threshold is reached, it is not clear what other options are available to Dublin Airport. We are of the view that the 33 million passengers per year is a rather arbitrary threshold and out of date. ✂[redacted].

7.36 ✂[redacted].

7.37 If the Commission decides to stick with the 33 million threshold, we would welcome confirmation that the price cap will change in the following year to reflect this. For example, we are looking for confirmation that the 2020 price cap would reflect this if Dublin Airport delivered 33 million passengers per annum in 2019. Similarly, we would also welcome confirmation that Box 2 will be depreciated over the remaining asset life as opposed to the actual asset life since remuneration is commencing approx. 10 years late.

8. Cost of Capital

8.1 Overview

8.1 In making its 2019 Determination, the Commission currently has statutory objectives '*to enable Dublin Airport Authority to operate and develop Dublin Airport in a sustainable and financially viable manner*' and '*to protect the interests of current and prospective airport users'.* [15] In this context, it is critical that the Commission sets an appropriate cost of capital for Dublin Airport for the 2019 Determination taking account of the high level of risk which the airport faces going into the next regulatory period.

8.2 We support the Commission's continued use of the Weighted Average Cost of Capital (WACC) method of calculating the regulated rate of return for Dublin Airport. This methodology involves calculating the cost of capital as the weighted sum of the cost of debt and the cost of equity based on the estimated returns that Dublin Airport would need to offer holders of debt and shareholders, respectively.

8.3 In setting its weighted average cost of capital for the 2019 Determination, Dublin Airport believes that the Commission's current pre-tax real WACC of 5.79% should be used as the starting point and any proposed changes in the current WACC parameters should be objectively justified.

8.4 It is important that the Commission's WACC calculation is grounded in empirical analysis and financial theory rather than simple benchmarks. However, where the Commission is required to use airport benchmarks for example in the case of measuring the asset beta, the benchmarks which are used must be suitable and objectively justifiable.

8.2 Cost of Equity

8.5 Dublin Airport suggests that the Commission considers the merits of taking a Total Market Returns approach (TMR) to the calculations of the risk-free rate (RFR) and equity risk premium (ERP) variables in the 2019 Determination.

8.6 A TMR approach involves measuring the total market return directly, and then calculating the constituent elements by subtracting the observed RFR (as proxied by government bonds) from the TMR estimate to derive an ERP. The TMR approach

[15] State Airports Act 2004, section 22, sub-section 4.

contrasts with an approach that estimates the ERP and RFR separately and independently. Empirical evidence shows that ERP and RFR negatively co-vary, e.g. with the ERP increasing during periods when monetary policy is loose and the RFR is low, as per current market conditions. A TMR approach ensures that the ERP and RFR are estimated jointly and consistently; by contrast, an approach that provides for independent estimation may provide for a total market return that is below investors' cost of capital.

8.7 A key factor which must be considered in estimating the TMR for the 2019 Determination is the potential impact of Brexit on financial markets. Brexit has led to increased volatility in European equity markets. This increased volatility supports an increase in the TMR to compensate investors for greater expected market volatility. This needs to be considered in the context of the Commission's cost of equity calculation.

8.8 We consider that the TMR should be estimated using the historical returns of long-run returns data. The Dimson, Marsh and Staunton ('DMS') database which is considered a very reputable source of income series data could be used for this purpose.

8.9 We are of the view that the risk-free rate should be calculated based on both long run data with evidence from a combination of Irish and Eurozone bond markets given that this will best reflect the business market in which Dublin Airport operates.

8.10 While Dublin Airport supports the estimation of the asset beta for airport using comparator data it is important that this estimate is based on robust comparator evidence and relative risk analysis. If a beta for a comparator airport is used as a reference point that this airport should be exposed to a similar risk profile as Dublin Airport. In order to determine the suitability of individual comparator companies for Dublin Airport, we need to consider key risk factors which affect systematic (beta) risk of companies operating in the airport industry.

8.11 We consider the following as the key beta risks that need to be considered:

- Airport demand, measured by passenger numbers or air traffic movements
- Revenue risks measured by
  - Aeronautical and non-aeronautical revenue splits
  - Composition of non-aeronautical revenues
  - Customer concentration
  - Passenger mix
- The regulatory framework in place (e.g. ability to adjust prices each year)

8.12 The Commission should consider how Dublin Airport's beta risks compare to the appropriate comparator airports that have been identified using the relevant criteria set out above. Based on an initial assessment of the comparator airports put forward by the Commission in its Issues Paper, Dublin Airport believes that a number of these airports would not be appropriate benchmark airports based on the above criteria.

8.13 In line with previous Determinations we will provide further evidence relating to this in our Regulatory Proposition, which is scheduled for December. We believe however that the burden of proof should not lie solely with Dublin Airport and that the Commission should provide sufficient objective justification to any reductions to the existing cost of capital parameters.

8.14 In addition to being guided by appropriate airport comparators to estimate the asset beta, we are of the view that it can be useful to take the existing asset beta value and examine whether the level of risk faced by Dublin Airport going into the next determination has changed since the equivalent period in preparing for the previous determination.

8.15 On this basis Dublin Airport believes that there is justification for an increase in the beta parameter in the 2019 Determination given the substantial amount of risk faced by Dublin Airport regarding its regulatory framework and its substantial capital investment proposals in addition to the uncertainty relating to the likely impact of Brexit.

8.3 Cost of Debt

8.16 The cost of debt can either be estimated directly from data on corporate bond yields, or it can be built up from its components which are the risk-free rate and a debt premium. While the former approach has the advantage of simplicity, the latter approach may be better suited to ensuring consistency with the risk-free rate assumption used in estimating the cost of equity. Dublin Airport favours a bottom-up approach.

8.17 We recommend that the cost of debt is estimated directly from data on corporate bond yields. Dublin Airport recommends that the Commission sets its cost of debt allowance based on Dublin Airport's embedded debt plus a forward-looking allowance for (expected) new debt costs. This approach will allow for the recovery of the efficiently incurred cost of debt, whilst taking into account the Irish business environment. Dublin Airport would support a full indexation of the cost of debt but understands that careful consideration needs to be given to the following factors:

- The categories of debt that should be included in the index.
- The credit rating of the bonds in the chosen index.
- The choice of data source.
- The time period over which data should be averaged in calculating the index.

8.4 Aiming Up

8.18 Given that it is widely accepted by regulators in Ireland and further afield that there is an asymmetry in consequences in estimating the cost of capital on the low side (i.e. where future capital investment is jeopardised) and setting a cost of capital on the higher side (i.e. where a marginally higher return would follow), we are of the view that the Commission should consider explicitly 'aiming up' on its estimated WACC allowance to safeguard against underestimating the future cost of capital value. In addition to future investments, financial viability and the interests of passengers is a key consideration in this regard.

8.5 Other Comments

8.19 While we acknowledge the downward trend in the value of the cost of capital allowed in recent regulatory decisions in the UK and Ireland, we do not believe that this trend is wholly applicable to Dublin Airport's prospective allowance for the following reasons:

- We are about to embark on a substantial capital investment programme which has a high degree of associated risk;
- Volume risk and regulatory risk needs to be considered;
- There is considerable uncertainty relating to the potential macroeconomic and traffic impacts of Brexit on Dublin Airport.

8.20 In addition, given the substantial level of risk faced by Dublin Airport in relation to its capital investment programme there is regulatory precedent to support a potential uplift to the WACC parameter to reflect this. Currently in the UK the CAA is considering recommendations made by its consultants PwC recommended the inclusion of an additional WACC premium in its costs of capital estimate to take account of the construction of the third runway at Heathrow Airport[16].

[16] http://publicapps.caa.co.uk/docs/33/PwC_H7InitialWACCrange.pdf

9. Financial Viability

9.1 Overview

9.1 In making its 2019 Determination, the Commission currently has statutory objectives '*to enable Dublin Airport Authority to operate and develop Dublin Airport in a sustainable and financially viable manner*' and '*to protect the interests of current and prospective airport users'*. [17] In order to achieve these objectives, the Commission must ensure the financial viability of Dublin Airport over the next regulatory period.

9.2 In ensuring financial viability over the next Determination period, the Commission must enable Dublin Airport to maintain its investment credit rating in order to minimise financial risk, access funding markets and raise debt at a reasonable cost and terms.

9.2 Testing Financeability

9.3 Financeability is determined in the regulatory context by examining whether or not the price cap resulting from the regulatory building block approach yields sufficient revenues to allow Dublin Airport to cover its operating expenditure, capital expenditure, depreciation and cost of capital while maintaining appropriate financial ratios from the perspective of investors and financial credit rating agencies. Ultimately, the implied credit metrics should imply a rating that is consistent with the rating underpinning the cost of debt and therefore cost of capital allowance.

9.4 The financeability test is used to provide an analysis of how much is being asked of Dublin Airport under the proposed regulatory determination. There are a number of reasons why a potential financeability gap could emerge between regulatory yields and financial requirements for a Dublin Airport over a regulatory control period.

9.5 A difference can emerge between the regulated company's actual market cost of capital and its allowed regulatory cost of capital. The market cost of capital measures the intrinsic riskiness of the company in terms of the cost of equity and of debt as perceived by the financial markets while the allowed regulatory cost of capital is traditionally equated to the WACC which is estimated using the CAPM model. While the theoretical model ignores regulatory risk, the financial markets demand an additional risk premium to compensate for the perceived impact of this additional risk.

[17] State Airports Act 2004, section 22, sub-section 4.

9.6 A financeability gap can develop due to the growing level of indebtedness of the regulated firm and the mismatch between the real returns earned by the regulated company on its RAB and the nominal interest which it pays on its debt. Dublin Airport is earning a real cost of capital and is compensated for inflation through an indexation of the RAB. However most firms are required to remunerate their debt investors through annual nominal interest payments based on ongoing inflation. This can result in a timing effect where the level of a regulated company's actual return on its assets is lower than the nominal costs of financing it.

9.7 A gap between revenues generated and debt repayments can have a significant effect on cashflows and resulting financial ratios for the regulated firm particularly where it is heavily reliant on debt. It is generally accepted that the issue of financeability becomes more acute the higher the gearing of the regulated company and the larger the capital investment requirement.

9.8 In the case of Dublin Airport, the Commission must examine the potential range of outcomes from its regulatory targets and price cap proposals for its 2019 Determination and ensure that no financeability gap is likely to emerge and that these regulatory proposals can allow Dublin Airport to comfortably maintain an investment credit rating. Where the outturn credit metrics are not consistent with the assumed rating underpinning the cost of capital, the Commission should consider the overall level of allowed revenues.

9.9 The Commission must address any case of an emerging financeability gap and there are a number of options available to the Commission, including:

- the provision of a revenue allowance over and above the level of revenues determined by the regulatory building block approach[18] which would directly compensate for a potential financeability gap and which would have the effect of increasing the present value of the regulatory company's revenue returns.
- the introduction of an accelerated depreciation approach through shorter asset lives for certain assets. However, by bringing forward cash-flows, this approach may simply defer financeability problems to subsequent reviews and may not therefore address fundamental financeability problems.
- Use of an 'aiming up' provision in the cost of capital to ensure that the regulated company is allowed an adequate return on investment to bridge any potential financeability gap.

[18] A financeability adjustment of this kind was used by the Commission in its 2009 Determination model

9.3 Dublin Airport's Financial Performance Since 2014

9.10 Dublin Airport's financial position has improved considerably since 2014 given that daa plc has now got a credit rating of A- from Standards and Poors in contrast to a BBB credit rating back in 2014.

9.11 Our financial risk has decreased since 2014, where based on the company's Regulated Accounts, Dublin Airport now has a FFO to Debt ratio of 30% (2017 Regulated Accounts) up from 11% (2013 Regulated Accounts) in 2013.

9.12 These financial results mean that Dublin Airport's notional rating would now be A- (the same as its daa plc rating) increasing from a BBB notional rating in 2014. daa has taken advantage of improved financial market conditions and the low interest rate environment in recent years.

9.13 daa went to the bond markets in 2016 to refinance its €550m bond which was due to mature in 2018. daa issued a €400m bond while also repurchasing €259.4m of this €550m bond at market rate where this meant paying the bondholders the interest which was due until final maturity. The remaining €290.2m of this original bond was repaid on 9 July 2018.

9.14 The coupon on the daa original €550m bond was 6.5872% but this debt has now been refinanced at the much lower rate of 1.554%.

9.15 The daa's €150m bank revolving credit facility was due to expire in December 2016, however daa succeeded in renegotiating this credit facility in November 2015, where the credit facility was extended to €300m and this facility now has a maturity of November 2022. The Group's strong investment grade rating has allowed this optimal financing to be executed.

9.4 Financial Outlook for Dublin Airport

9.16 daa is operating as a fully commercial company with no recourse to the Exchequer for funding or equity injections. In March 2017, the daa Board approved a dividend policy which provides for an annual dividend payment to the Government of between 30% and 40% of normalised profit after tax subject to the priority that daa plc can maintain a minimum credit rating of BBB+.

9.17 It is envisaged that in order to fund our proposed capital investment and to maintain its existing operations at Dublin Airport, ✂[redacted].

9.18 This means that daa is going to be required to double its current net debt [redacted].

9.19 daa will potentially be seeking to raise this new debt for Dublin Airport in the next regulatory period, from the European Investment Bank, bond markets and other appropriate sources.

9.20 Given that daa is going to be heavily reliant on funding airport development in the next regulatory period, Dublin Airport will need a balanced regulatory regime that is perceived by debt providers as fair with safeguards in place to ensure that investors will have confidence in lending to daa to fund capital investment at the airport, particularly with respect to long term financing.

9.5 Assessing Financeability in the 2019 Determination

9.21 We support the Commission's continued use of credit rating metrics to assist in its assessment of financeability for Dublin Airport.

9.22 The Commission's use of credit rating metrics is appropriate given that this is the benchmark which is replied upon by funding markets to assess a company's credit profile and overall financial viability.

9.23 We believe that it will be important for the Commission to look at the notional credit rating for Dublin Airport in examining financial viability under the 2019 Determination.

9.24 We recommend that in assessing financeability for the 2019 Determination, that in addition to setting a credit rating metric, the Commission should carry out a full quantitative assessment of the likely impact of its different regulatory targets, the various possible regulatory risks and the business environment in which Dublin Airport operates.

9.25 This is particularly important for the 2019 Determination, given the increased scale of Dublin Airport operation, the required level of capital investment going forward, the potential impact of Brexit, the medium-term outlook for capital markets and the disproportionately higher risks faced by Dublin Airport which may leave daa consequently more financially exposed than in previous years.

9.26 In this context as a safeguard for financeability, Dublin Airport is recommending that the Commission includes an 'aiming up' element in its cost of capital assessment, as detailed in Section 8.4 above.

9.27 While Dublin Airport does accept that its financial conditions have notably improved since 2014, however given the unprecedented level of risk faced by Dublin Airport going into the 2019 Determination it is concerned that the use of an investment grade BBB credit rating metric will no longer be adequate for ensuring financeability.

9.28 Maintaining a strong investment grade credit rating (minimum BBB+) is essential for Dublin Airport to maximise the likelihood of debt market access and achieve competitive refinancing terms, improving daa's protection against financial risk.

9.29 A target credit rating of BBB+ would be consistent with precedent in other regulated sectors in Ireland where in its 2017 pricing decision for gas networks the CER based its financeability test on allowing for an investment grade with some degree of headroom[19].

9.30 Therefore, Dublin Airport would recommend that in assessing financeability for the 2019 Determination, the Commission should use a target credit rating of BBB+ to allow headroom in ensuring that the daa is allowed to operate Dublin Airport in a sustainable and financially viable manner.

[19] https://www.cru.ie/wp-content/uploads/2017/06/CER17260-PC4-CER-Transmission-Decision-Paper.pdf

10. The Commission's Service Quality Regime

10.1 Overview

10.1 We have demonstrated why service quality needs to be given due consideration by the Commission in the previous sections on operating expenditure, passenger growth, infrastructural development and the overall regulatory approach.

10.2 Regarding passenger representation, we refer to our respective responses to the Commission's consultations on this matter dated 16 October 2017[20] and 9 February 2018[21].

10.3 Below we have set out perceived shortcomings with the Commission's service quality regime in place at Dublin Airport and request that the Commission re-evaluates the effectiveness of an outdated security queue target. In addition, we demonstrate the need for a more flexible approach and have provided relevant international context from a service quality point of view.

10.2 Shortcomings with the Commission's Approach

10.4 As set out by the Commission in paragraph 11.1 of the Issues Paper consultation, its objective is to incentivise Dublin Airport to achieve efficient cost levels. Relating to this, it introduced a quality of service regime in 2009 that helps to ensure that the cost efficiencies achieved by the Airport are not made at the expense of the quality of service for users.

10.5 Furthermore, in paragraph 11.2, the Commission notes that the regime is in line with its statutory objective to protect the interests of current and prospective users of Dublin Airport and that this regime is also supported by the 2017 Policy Statement on Airport Charges Regulation, which states that regulation should ensure that passengers are presented with choice, value and quality services.

10.6 We have a number of issues with the Commission's approach set out above and particularly with the 30-minute maximum security queue target which the Commission has referred to as being the most important measure in terms of allowed revenue at risk.

[20] http://www.aviationreg.ie/_fileupload/2017/17-10-16%20Dublin%20Airport.pdf
[21] Not currently published by the Commission but submitted to the Commission by email.

10.7 It is not clear how the 30-minute maximum security queue target is in and of itself targeted at ensuring our overall costs achieved would have been greater had this regime not being in place. In fact, we endeavour to have a queue time that is far less than the 30-minute threshold set by the Commission so from that perspective alone, the 30 minutes can be viewed as a rather arbitrary threshold.

10.8 We are firmly of the view that the Commission should consider that the financial penalty associated with the security queue exceeding a certain time is somewhat at odds with security regulations that emphasise the need to prioritise rigour when processing passengers. We essentially have one regulation stipulating the need to come in under a certain time and separate regulations that suggest that the safety of passengers should not be compromised under any circumstances.

10.9 While we prioritise the safety of our passengers at all times, we are of the view that the Commission should consider amending the conditions under which a financial penalty would be incurred to reflect extreme outliers. We are of the view that this target becomes less of an issue if we are required to meet the sub 30-minute threshold 99.X% of the time.

10.10 Dublin Airport requests that the Commission demonstrates empirically how the quality of service regime is working as intended and to reassess whether any improvements can be made to the existing service quality regime.

10.11 Moreover, the Commission's reference to the 2017 Policy Statement on Airport Charges Regulation is lacking substance. The quality of service regime has been in place for years before this statement in order to supposedly "*ensure that the cost efficiencies achieved by the Airport are not made at the expense of the quality of service for users*" rather than to ensure "*that passengers are presented with choice, value and quality services*". Overlooking the status of the proposals within this 2017 document, the Commission's position on the quality of service regime appears to be somewhat disjointed.

10.12 The consequences are very significant for Dublin Airport as it incurs significant financial penalties that are not necessarily effective at achieving what they are intended to, as set out by the Commission (detailed above).

10.3 Specific requests of the Commission

10.13 In addition, the Commission has set out in paragraph 11.3 of the Issues Paper consultation that it is mindful of these quality targets (and presumably the financial penalties by extension) when setting other building blocks. Dublin Airport requests more explicit transparency from the Commission in this regard.

10.14 Related to our requests in paragraph 10.10, we specifically request that the Commission reconsiders the 30-minute maximum security queue target that is in place all of the time in both terminals.

10.15 More generally, we wish to acknowledge the leeway provided by the Commission during storm Emma in Q1 2018 and during previous red alert weather warnings. We believe that a more formal approach taken in this regard would lead to efficiencies and improve the safety of security staff who may otherwise be at risk during such extreme weather events i.e. it may not always be possible to receive confirmation from the Commission in real time that an existing weather event is grounds for an exemption.

10.4 Recent developments necessitating a more flexible approach

10.16 There have been a number of key developments related to this target since it was first introduced by the Commission. For example:

i. The terminals are more capacity constrained which has been clearly demonstrated by the PACE consultation process. This means that the targets have become more difficult to meet relatively to when the initial years following their introduction.

ii. Any extra security measures such as the introduction of Explosive Trace Detection for both passenger and cabin bags adds to the complexity of the security process and requires more time.

iii. Certain new policies introduced by airlines (e.g. Ryanair) has resulted in luggage coming through security that might otherwise have been checked-in.

10.17 In this regard and in the context of the Commission's Table 11.1 in the Issues Paper, it is worth noting that there have been a number of breaches in 2018 already, with a strong possibility of further breaches. It follows from the above that a more flexible approach should be agreed.

10.18 We are of the view that due to the extent to which certain circumstances are beyond our control coupled with more stringent (and somewhat conflicting) security regulations which have the effect of further delaying the throughput, the Commission should consider a target that is in place 99.x% of the time i.e. Dublin Airport should be afforded a number of specific exemptions per year in which the median time exceeds 30 minutes. It is worth exploring alternative more innovative and effective solutions.

10.5 Disproportionate emphasis currently placed on penalties for under-performance

10.19 The current regulatory framework includes quality of service targets with no reward for outperformance but penalties for under-performance. We are keen for the Commission to consider both the case for a more explicit link between quality of service targets and the Opex allowance and the case for rewards for outperformance.

10.20 Ofwat has explicit links between quality of service targets and cost allowance. Water regulation follows an outcomes-based framework and the delivery of customer outcomes is monitored through a review of Outcome Delivery Incentives (ODI, or equivalently measures of outperformance). Water companies set out their cost allowance requirements to deliver the outcomes valued by their customers (including meeting the ODI targets) in their business plan submitted to Ofwat. Their setting of targets reflects the result of research on customers willingness to pay for a given standard of service delivery.

10.21 While a number of ODIs are subject to penalties for under-performance, this regime also allows for outperformance rewards that is supported by customers evidence showing support for incremental gains in quality of service.

10.22 The Commission has referenced in its Issues Paper the upcoming outcomes-based framework to be adopted for the next price control of Heathrow airport in the UK. This approach is intended to create a link between the cost allowance and the activities that are necessary to deliver the outcomes and the targets on measures of performance. A strong emphasis is placed on the customers evidence that shows support for the outcomes (i.e. the most important aspects of the airport's services that consumers value), the targets and the value of the financial incentives.

10.23 The current Service Quality Rebate and Bonus ('SQRB') scheme in use at Heathrow is not a penalty-only scheme. The scheme includes a bonus element on passenger satisfaction measures to reward high performance that benefits passengers. The maximum additional revenue achievable via bonuses at Heathrow is 1.44% of airport

charges[22]. The indicators with a bonus element for outperformance include departure lounge seat availability, cleanliness, wayfinding and flight information.

10.6 How Dublin compares internationally on service quality

10.24 In 2015, Dublin Airport joined a new 'Category 1' peer group in the ACI Airport Service Quality ('ASQ') scores. It is evident that our peers have made significant improvements with competition in this top tier intensifying. Our Airport was ranked fifth in Q4 2017 but this represented our lowest ranking since the beginning of 2013. Furthermore, in Q1 2018 we dropped outside the top five and were eight in the rankings.

10.25 Behind this trend is a more positive and stronger performance of our peer airports in the eyes of passengers. While passenger satisfaction at Dublin Airport remains quite good with respect to staff, car parks, washrooms and baggage delivery, there is some concern regarding the experience at the departure gates and ease of connecting flights.

Table 4: [redacted]

[redacted]	[redacted]	[redacted]	[redacted]
[redacted]	[redacted]	[redacted]	[redacted]
[redacted]	[redacted]	[redacted]	[redacted]
[redacted]	[redacted]	[redacted]	[redacted]
[redacted]	[redacted]	[redacted]	[redacted]
[redacted]	[redacted]	[redacted]	[redacted]
[redacted]	[redacted]	[redacted]	[redacted]
[redacted]	[redacted]	[redacted]	[redacted]
[redacted]	[redacted]	[redacted]	[redacted]
[redacted]	[redacted]	[redacted]	[redacted]

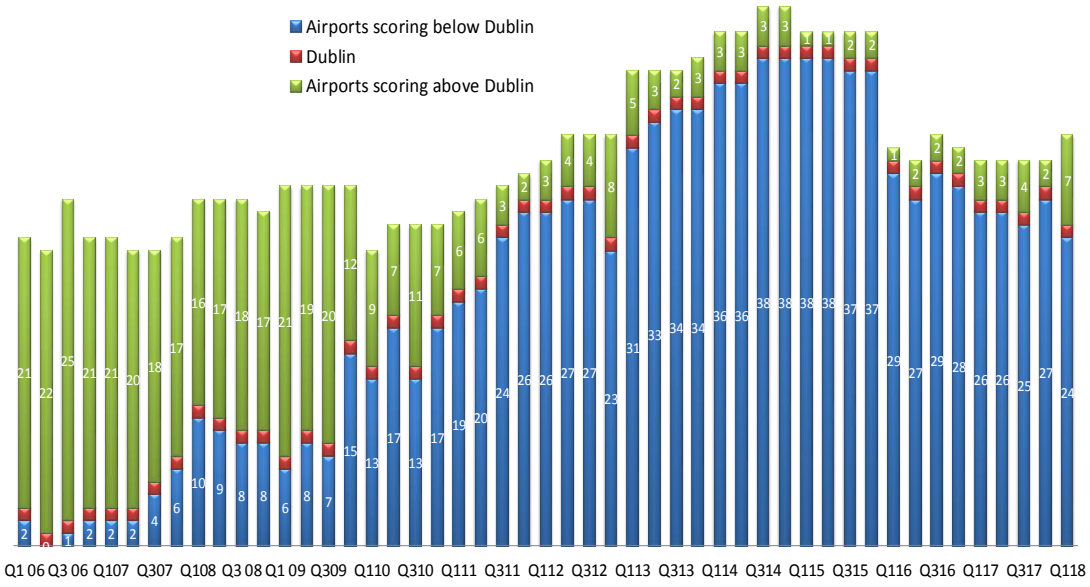
[22] https://www.heathrow.com/company/company-news-and-information/performance/airport-operations/service-quality-rebate-and-bonus-scheme . The indicators with a bonus element for outperformance include departure lounge seat availability, cleanliness, wayfinding, and flight information.
https://www.heathrow.com/file_source/Company/Static/PDF/Companynewsandinformation/LHR_SQRB_May18.pdf

10.26 The following factors are worth considering in the context of the lower ranking in 2018:

- The works in Piers 3 and 4 which are placing additional pressure on facilities;
- Growth in the 50-64's passenger profile and the additional holiday groups, which have previously tended to be more critical with respect to service quality;
- ✂ [redacted];
- ✂ [redacted];
- ✂ [redacted].

10.27 Indeed, the main 'upgrades' coming through in the ACI ASQ scores in the well performing airports are notably in facilities, ease of movement, security and airport ambience.

Figure 8: Airport Council International Airport Service Quality Scored Q1 2018



10.28 In order to maintain a good passenger experience, Dublin Airport has implemented a passenger journey management programme comprising a cross functional team that focuses on driving improvements in passenger satisfaction, which seeks to identify and deliver projects to enhance the passenger experience in the short term.

10.29 However, it is clear that for Dublin Airport to continue to successfully compete with Category 1 Airports, the Commission needs to have due regard for service quality and passenger experience when considering the appropriate operating expenditure allowance and the nature of the capital investment programme. Furthermore, financial penalties for reductions in service quality are not a panacea, given that Dublin Airport is accommodating increasingly numbers of passengers in a more constrained environment.

✂ [redacted]

[redacted]

✂ [redacted]

[redacted]

✂ [redacted]

[redacted]

✂ [redacted]

[redacted]

10.7 Augmenting the Commission's service quality regime

10.30 Regarding the Commission's question in paragraph 11.42 of the Issues Paper on the inclusion of arrival measures in the quality of service regime, we wish to refer the Commission to our responses to consultations in October 2017 and February 2018 regarding passenger engagement and representation. Specifically, we are keen for the Commission to demonstrate that the costs do not exceed the benefits.

10.31 Finally, there is insufficient information provided by the Commission for us to meaningfully comment on its proposals in paragraph 11.43 of the Issues Paper relating to immigration inspection.

10.32 Is the Commission suggesting that Dublin Airport should incur financial penalties for delays in immigration queues, similar to departing security queues, even though Dublin Airport is not responsible for operating immigration and border control?

10.33 The Commission has rightly noted that immigration and border control is operated by the Irish Naturalisation and Immigration Service (INIS), which is part of the Department of Justice and Equality.

10.34 Furthermore, the Commission has correctly noted that Dublin Airport may influence the experience in immigration and the Commission will be acutely aware that we are very active in this regard, which has been demonstrated in the recent PACE consultation process.

11. Other Issues

11.1 Passenger Engagement

11.1 The 2017 National Policy Statement on Airport Charges Regulation places the passenger at the centre. We would welcome guidance from the Commission on how this will (if at all) impact the 2019 Determination and how best we can prepare in this regard.

11.2 We have already stated in paragraphs 3.7-3.11 why service quality needs to be a key consideration by the Commission when setting the respective building block targets. Ultimately the passenger experience and interest will be dictated by the level of service quality on offer, which comes with a cost.

11.3 Regarding passenger representation, we refer to our respective responses to the Commission's consultations on this matter dated 16 October 2017[23] and 9 February 2018[24].

11.2 K-Factor

11.4 The k-factor affords Dublin Airport with important pricing flexibility as noted by the Commission in CP2/2015 which states that "*The objective of the k factor is to allow Dublin Airport some flexibility on pricing, in particular to mitigate a potential situation where towards the end of the year Dublin Airport is not going to reach the price cap without changing prices mid-season*."

11.5 As set out by the Commission in paragraph 12.17 of the Issues Paper, the k factor mechanism recognises that Dublin Airport cannot set prices to hit the cap perfectly due to the charging structure in place. Dublin Airport continues to subscribe to this view and would not be in favour of abolishing the k factor due to the complexity and assumptions required when forecasting annual revenues.

11.6 Dublin Airport's published suite of airport charges is extensive and more complex than a price cap charge per passenger. Pricing is dependent on the season, summer and winter in accordance with IATA. However, price cap compliance assesses aeronautical

[23] http://www.aviationreg.ie/_fileupload/2017/17-10-16%20Dublin%20Airport.pdf
[24] Not currently published by the Commission but submitted to the Commission by email.

revenue charged in the financial year i.e. January to December. Therefore, Dublin Airport proposes charging for three different seasonal periods;

- Current winter season;
- The following summer season, and
- The following winter season.

11.7 Additionally, charges are related to the usage of certain facilities, such as; runway, parking, airbridges, passenger service charges etc. Thus, several estimates are required to accurately forecast net revenues for the pricing year (January to December), which then require compliance with the allowed price cap by passenger (actual passenger out-turn).

11.8 The current pricing year is used as the base for forecasting the forthcoming pricing period, as it is the most accurate data available for:

- Profiling passengers e.g. departing, arriving, point to point, transfer, transit etc.
- Usage and consumption of facilities e.g. contact vs remote stands, fast-track usage, PRM etc.
- Uptake and compliance with incentive schemes e.g. route support, GROWTH, transfer, behavioural discounts etc.
- Movements by type of aircraft e.g. MTOW required for runway charge and number of movements required to estimate parking charges.

11.9 In addition to the above factors, other considerations are required for forecasting passenger traffic, such as:

- Gross Domestic Product (GDP) expectations for the pricing year;
- Incorporation of any new or expanding business activity, based on market intelligence and insights; and
- Incorporation of additional frequencies on routes and/or expected changes in aircraft gauge for the forthcoming summer season.

11.10 On an annual basis, all assumptions will vary from those budgeted. Tight oversight and control of revenues is required to ensure revenues collected are a minimum of 95% of the price cap and no more than 100% of the price cap allowed.

11.11 ✂ [redacted]

[redacted].

11.12 The level of risk with Dublin Airport on price cap compliance is already asymmetrical as if Dublin Airport over collect, a refund is due shortly afterwards whereas if Dublin Airport under collects, a two-year delay period is in place. The Commission's ask to users on whether the k factor mechanism should remain in place at all further exacerbates the risk to Dublin Airport. Commitment can be given on timing of Grow payments if that gives users more pricing certainty however the annual level of Grow fluctuates until the passenger numbers close for a financial year.

11.13 We would like to highlight that only 45% of users submitted passenger traffic for the 2018 price consultation process, leaving Dublin Airport to make significant passenger traffic assumptions when setting price levels. To date, traffic levels are above targets and impact on revenue levels collected.

11.14 The Commission must give due consideration to any significant changes to the k factor. In the event the k factor mechanism was removed, it would likely result in a situation where Dublin Airport would exceed the price cap set in order to ensure 0% under-recovery. Dublin Airport is not supportive of this as it results in less revenue certainty for the airport and airlines.

11.15 We therefore request that the k factor mechanism remains in place. In accordance with paragraph 12.25 of the Issues Paper we believe that the Commission should implement Option 1 whereby it adjusts the k factor based on outturn passenger numbers, and an updated forecast for passenger numbers ahead of the year in question. We agree that there is merit in removing the volume impact on the k factor as that is not the intention of the mechanism i.e. the value of the mechanism is wider – pricing certainty, flexibility and compliance. It follows that a fixed K Factor would be set in the provisional price cap statement published by the Commission each November. This would reduce the extent of volume risk in the K Factor.

11.3 Route Incentives

11.16 The Commission has raised a relatively short question on route incentives but it is simply not appropriate to address the Commission's question in this context. Specifically, the Commission fails to provide an adequate (indeed any) definition of "incentives", or any useful definition of the terms "cross subsidy" or "self-funding". Without these terms well defined it is not possible to have a coherent debate on the functioning and economics of incentive schemes.

11.17 Our incentive schemes are designed with a number of specific objectives in mind:

- To make most efficient use of the airport infrastructure in the short, medium and long run;
- To maximise traffic at the airport;
- To increase the connectivity offered at Dublin (routes and frequencies).

11.18 All airlines and passengers benefit from the pursuit of these objectives, while all of our schemes are transparent and non-discriminatory.

11.19 We reject the Commission's simplified approach to the issue of what it terms "cross subsidies" in the connect of incentives and the suggestion that incentives should be treated as non-recoverable Opex. If such a rule were to be applied it would undoubtedly result in less efficient use of airport infrastructure resulting in lower traffic growth and higher capacity spending in the long run and. Both would result in increasing average aeronautical charges overall.

11.20 Concerning our behavioural incentives, these induce airlines to make more efficient use of scarce airport infrastructure, and so reduce our costs in the long run. As such all users benefit from these incentives. Furthermore, the Commission's suggestion that these charges should be "self-funding" in the way described is nonsensical. The services affected by these charges are close substitutes, e.g. contact and remote stands. As is well known from the economics of common costs, efficiently differentiated pricing for services which are to some degree substitutable leads to higher demand overall and an increase in consumer welfare. The extent of price differentiation may reflect differences in incremental cost or different customer demand elasticity. In a regulated setting, the productive efficiency gained as a result is passed-through to customers in lower prices in the medium term.

11.21 By way of example, our Long Haul Remote Arrival Discount encourages long haul operators to place morning arrivals on remote stands, making more space for other operators at contact stands. If the operator continues to use a remote stand they will continue to get the discount. If they revert to contact stands they cannot be charged more than other operators. But all operators benefit from the freeing up of contact stands. Hence the current arrangement that amounts to a marginal rebalancing of charges between different aircraft stand options is justified.

11.22 Generally, the Commission's suggestions do not reflect the reality of an airport, which like network industries uses a common infrastructure to serve many different customers and markets.

11.23 Economic theory dictates that the overall welfare of airport users is maximised if contributions to infrastructure costs are made in proportion to the *value* users place on that infrastructure. Our growth and new route incentives essentially amount to a rebalancing of the structure of tariffs between existing and new/growing traffic in a way that is justified in economic terms and induces greater traffic and connectivity growth. Growing traffic, including the development of new routes and the provision of additional aircraft, presents greater commercial risks to airlines than simply continuing to serve the same routes using the same aircraft capacity. Therefore, it is economically rational for airports to offer rebates to encourage traffic growth and the discounts to airlines that take the chance of operating new routes relative to established routes. Nevertheless, it is reasonable for runway and passenger charges in their entirety to cover the reasonable costs of those services. In the medium-term airlines operating at Dublin benefit from the growth and route incentives because traffic growth, tends to reduce average charges per passenger.

11.24 The Commission's model of self-funding incentives is neither consistent with good airport economics nor is it feasible. We cannot "recover" previous discounts through higher charges to specific carriers once a route is established. Once a carrier has taken the risk of establishing a new route and proved its viability such a pricing policy would leave that carrier exposed to unfair entry from another carrier that would not have to pay the increased charge. Similarly expecting to recover the "cost of incentives" simply through greater a greater volume of traffic from the recipient airlines is not possible either, because the airport cannot expect to earn a higher rate of profit on incremental traffic, because this will be regulated away at the subsequent price control. Nevertheless, incentives for growth and increased connectivity are self-funding, and so justified in the sense that they increase overall use of the airport leading to lower charges on average for all airlines.

11.25 There are many instances in which airlines have demonstrated their support for the incentive Schemes in place at Dublin Airport ✂[redacted]:

[redacted]

11.26 Furthermore, at the most recent Airport Charges Consultation we recall only one airport user expressing an issue with how incentives were funded with no airport user expressing any issue with the presence of incentives.

11.4 Necessary CIP Overspend and RAB Roll Forward

11.27 This section details relevant expenditure incurred by daa in providing necessary projects to ensure safe and sustainable operations at Dublin Airport. They haven't been included in PACE as they are not necessarily capacity enhancing projects, which was a requirement of PACE. Instead, these projects reflect, for example, necessary and significant scope changes not previously envisaged in addition to satisfying safety requirements. Ultimately this expenditure is above and beyond the flexibilities that CAR has provided in the CIP groupings, when necessary spend for 2018 and 2019 is accounted for. We are in a position to provide more information on these projects and the process, as required.

✂**Table 5:** [redacted]

[redacted]

11.5 Runway 10/28 Overlay

11.28 This comprised a number of interrelated projects within the Airfield Maintenance category associated with Runway 10/28. We realised that significant economies of scale could be achieved from combining a number of Runway 10/28 projects with the main overlay project. The runway and some key taxiway pavements were in need of their first major rehabilitation since opening in 1989. A less expensive repair option called a Thin Porous Friction Course ('TPFC') was undertaken in 2010-2011, this comprised overlaying the Runway with a thin 22mm layer of asphalt which had a life of 6-8 years. It sealed the surface of the concrete pavement and prevented water ingress, which prevented further issues.

11.29 The TPFC did not increase the structural life of the runway but prevented further accelerated deterioration for a short period. Towards the end of life on the TPFC, cracking appeared on the surface which required immediate intervention in the form of joint repair and sealing to prevent Foreign Object Damage. In 2014 a structural evaluation was undertaken which indicated that the structural life of Runway 10/28 had already been exhausted. At the time of the preparation of the current CIP, 21.4m passengers were projected for 2016. The actual passenger throughput that materialised was almost 28m. Finally, these works will extend the life of the runway by approximately 15 years.

11.6 Hi Mast Lighting Upgrade

11.30 The High Mast Lighting Upgrade project was a key component of Dublin Airport's transition application from the existing national aerodrome licence to the EASA

European Certificate. The non-compliance with regard to EASA CS M.750: Apron Floodlighting, (horizontal illuminance — 20 lux with a uniformity ratio [average to minimum] of not more than 4 to 1) was treated as a Deviation Acceptance and Action Document ('DAAD') as part of Dublin Airport's overall EASA transition application. This project addressed the non-compliance issue with 71 high mast lights ensuring Dublin airport was in compliance with EASA standards and therefore retaining its operating certificate.

11.7 Masterplan

11.31 The previous Dublin Airport Masterplan was prepared in 2008 by Pascall & Watson Architects and whilst it had a horizon of 52mppa, it focussed primarily on taking Dublin Airport from c.20mppa to c.32mppa. Since that masterplan was prepared, considerable policy and operational changes had occurred to Dublin Airport including:

- Significant long-haul route expansion to Africa, the Middle East, North America and Asia (including mainland China);
- Change of business strategy with significant growth in transfer traffic;
- Changing airline business models with Ryanair adopting strategies associated with more full-service carriers;
- Continuing technological advances along with changing passenger behaviour (e.g. by-pass of check-in in favour of online check-in);
- Continuing advances in aircraft type and technology (e.g. new large aircraft and short haul aircraft with long range capabilities);
- Changing external environment including regulatory (safety), legislative (e.g HBS) and policy (e.g. new metro north).

11.32 It is important to ensure that the baseline foundations of a Masterplan maintain relevance in order for it to be effective. Over time these will change, and Masterplan updates are required to address this. In order to ensure Dublin Airport developed in the most efficient way possible it was necessary to update the 2008 Masterplan from a business perspective.

11.8 Taxiway Re-Designation

11.33 This project involves the re-designation of Taxiway Signage on the airfield as part of the Air Accident Investigation Unit Report, IRL00911044, issued in 2012 following a Monarch Airlines incident in May 2011. The recommendation from this report is highlighted below. The review, including consultation with stakeholders, following this report was completed in 2015, and this resulted in re-designation of the taxiway network to simplify taxi instructions. This approved signage re-designation scheme is

being gradually rolled out through the airfield and the cost of ✂€[redacted] is to account for work completed in this current CIP period. The benefit of this project is less potential for error in pilots interpreting ATC communications.

4. SAFETY RECOMMENDATIONS

It is recommended that:

1. Dublin Airport Authority in conjunction with the Irish Aviation Authority should review taxiway designation at EIDW in order to simplify taxi instructions. IRLD2012005
2. The Dublin Airport Authority considers aligning taxiways F1 and F2 in order to reduce complexity at their intersection. IRLD2012006

View Safety Recommendations for Report 2012-017

11.9 MV Cable Replacement

11.34 The airfield MV electrical ring main cable dates from the late 1980's and was of the old paper insulated type. In recent years concern grew regarding the reliability of this old cable type which runs the full length of the south side of Runway 10/28 and 2/3rds of the north side of the runway before turning to run along the West Apron to the Fire Station.

11.35 The cable is critical to providing the main electrical supply to our Airfield Ground Lighting systems (AGL) with any disruption having the ability to seriously impact airport operations both during daylight hours and particularly at night.

11.36 The AGL system comprises all runway and taxiway lighting plus airfield signage. Over the years with many changes to airside infrastructure, there are now a number of cable joints which are primarily 'transition joints' that join two different types of MV cable together.

11.37 These transition joints are more prone to failure compared to joints of identical cable types. The project comprised the essential replacement of 3 sections of end of life MV electrical cable on the south side of Runway 10/28 serving the AGL system.

11.10 Departures Floor

11.38 The Departures floor in Terminal 1 was being upgraded to replace end of life flooring and to uplift the check-in areas by providing a bright, light and tiled floor surface. This project also ensured a consist flooring style throughout Terminal 1 matching the

arrivals floor upgrade. It was also a key enabler for relocating airlines from Terminal 2 to Terminal 1, which had not been previously envisaged.

11.39 ✂ [redacted].

11.11 Repairs to the Departures Road

11.40 This project comprised the sealing and waterproofing of the Terminal 1 Departures Road to prevent water ingress to the underlying structure thereby preventing more serious structural failure. The road surface was removed down to the deck structure which was then sealed to protect the structure from corrosion and to remove leaks into the Terminal 1 Arrivals Level.

11.41 Following a structural survey carried out in 2012 by Punch & Partners, Structural Engineers, a report was issued in January 2013 recommending repairs and associated waterproofing to be carried out as a matter of priority, to limit the damage to the structure from the Departures Road (essentially a bridge deck) built in 1971[25]. The consultant recommended completing the works in one single phase by closing the Departures Road, in order to ensure the best quality of waterproofing installation. The Departures Road was closed for a period of time and the works were completed, adverting more serious structural issues being necessary.

11.42 Waterproofing on the road was identified as failed together with the lack of suitable pavement crossfalls, long falls and numerous construction joints leading to significant water leaks into the structure and into the occupied areas below (Arrivals concourse). The problem was being managed by addressing each leak as they occur through temporary repairs and redirection of water. This was not a long-term solution with a complete upgrade of the Departures Road providing the only suitable solution to the poor condition of the road and associated leaks.

[25] We acknowledge that the repairs to Departures Road was included in the previous Determination and that the Commission did not provide for an additional allowance in this Determination. However, we request that the Commission considers events that have taken place since this Determination was finalised and the recommendations that were issued by the structural engineers. We are in a position to provide more information as required.

11.12 T1 Critical Equipment Upgrades

11.43 Funding under this category is made up of a number of individual projects with a CIP allowance of €6m. A key safety/regulatory projects within the T1 Critical Equipment allowance was the Life Safety Systems ('LSS') comprising smoke detectors, alarms, emergency lights and associated cabling within Terminal 1.

11.44 Following the 2014 Determination it became apparent that the funding required for this project would be significantly higher than that allowed for in the CIP. There was a need to upgrade end of life equipment to ensure that Dublin Airport remained compliant with fire safety regulations and given more recent events (i.e. the Grenfell Tower tragedy in London and the Metro Hotel fire in Ballymun) which were key considerations in delivering Phase 3 of this project. To ensure the necessary standards were achieved in the terminal on all floors there was a need to spend ✂€[redacted]m on 3 phases of the LSS project. This was ✂€[redacted]m over the original allowance of €0.7m accounting for the majority of the overspend in the T1 Critical Equipment category.

11.13 Pier 1 Ground Floor Alterations

11.45 During the early stages of the 2014 Determination passenger growth accelerated ahead of expectations. Growth was being delivered across a range of carriers including Ryanair. Ryanair base the majority of their operations from Pier 1 and as a result of forecasted growth it became apparent that there were insufficient gates on Pier 1 to accommodate Ryanair based aircraft. This project delivered on one additional gate in Pier 1 and allowed for the conversion of 2 remote parking stands to walk out stands as a result of the new gate. The project also enabled less towing from remote stands during peak times on what is a congested airfield. ✂[redacted].

11.14 Preclearance Lounge

11.46 This pre-clearance lounge (51st & Green) was built to ensure that Dublin Airport enhanced its US Customs Boarder Protection (CBP) product. While there was a business case which influenced the delivery of this project, the Commission will consider future revenues from this facility and therefore we are of the view that the Commission should also consider the costs or a proportion of these costs.

11.47 This project was fast-tracked to ensure Dublin remained competitive for Transatlantic passengers in both the business and transfer markets.

11.48 The Lounge was built on the ground floor at the end of Pier 4 providing a relaxing environment for Transatlantic passengers wishing to avail of this facility. The revenue that will be generated from this facility will offset the aeronautical costs at Dublin Airport and an allowance is warranted on this basis.

11.15 Passengers with reduced mobility

11.5 In paragraph 12.8 of the Issues Paper consultation, the Commission has noted the two options proposed by Dublin Airport that can rectify the existing issues associated with the PRM formula. One option involves the PRM charge being outside of the price cap with the other option (with two sub-options) being to improve the charge while keeping it inside the price cap.

11.6 Under a scenario where PRM costs would come out of the price cap, revenues would be collected separately on a cost-related basis. To provide context regarding how this would work, 2019 pricing would include an adjustment for the estimated cumulative under-recovery to 2018. From 2020, Dublin Airport would estimate a charge for the year and communicate to airport users within the same time frame as the airport charges consultation.

11.7 We have proposed two options related to the PRM charge staying within Price Cap with a corrected formula set out below.

11.8 Under Option 1 with PRM staying within the price cap, 2019 pricing would ignore the cumulative under-recovered costs to the end of 2017. From 2020, Dublin Airport would take the cumulative under-recovery from the last audited financial statements from two years prior (e.g. 2020 will look at 2018).

11.9 Under Option 1 with PRM staying within the price, Dublin Airport would ignore the cumulative under-recovery to the end of 2018. This cumulative under-recovered amount will remain in the PRM statements. From 2021, Dublin Airport will take the cumulative under/over-recovered amount into the calculation from two years prior (2019), less the net cumulative 2018 under-recovered position.

11.10 Our preference is for PRM to be taken out of the price cap as it is artificially inflating the airport charges incurred by airport users.

11.11 We also request that the Commission considers the merits in removing the HBS operational costs from the price cap while ensuring that Dublin Airport is sufficiently remunerated through an alternative channel.

11.12 We look forward to receiving guidance from the Commission in relation to the above. If possible, we would appreciate clarity by August in order to allow sufficient time to prepare for the 2019 Airport Charges Consultation in Q3/Q4 of this year.

11.16 Other issues that may arise

11.13 We understand that the Commission has a particularly busy schedule in advance of the next Determination and that certain submissions, including responses to the Issues Paper, are required in a timely manner. While we have responded to the Issues Paper by 13 July 2018, as requested by the Commission, we wish to have an opportunity to raise any material issues with the Commission for consideration in advance of the Draft Decision that is expected to be published in April 2019.

11.14 Similarly, we believe the process would benefit from the Commission taking the opportunity to update stakeholders with any relevant information in advance of publishing the Draft Decision as this will lead to a more effective process.